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KOREA

STAFF APPRAISAL REPORT

THE KOREA DEVELOPMENT BANK IV

November 20, 1980

Projects Department  
East Asia and Pacific Regional Office

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### CURRENCY EQUIVALENTS

	<u>Prior to 1/12/80</u>	<u>From 1/12/80</u>
US\$1.00	= Won 485	Won 580
US\$1 million	= Won 485 million	Won 580 million
Won 1	= US\$0.0021	US\$0.0017
Won 1 million	= US\$2,062	US\$1,724
Won 1 billion	= US\$2.06 million	US\$1.72 million

### ABBREVIATIONS

ADB	-	Asian Development Bank
BOK	-	Bank of Korea
CNB	-	Citizens National Bank
DMB	-	Deposit Money Bank
EPB	-	Economic Planning Board
ERR	-	Economic Rate of Return
Exim Bank	-	Export Import Bank of Korea
FRR	-	Financial Rate of Return
GNP	-	Gross National Product
GRA	-	Guarantee Release Arrangement
IFC	-	International Finance Company
IFD	-	Industrial Finance Debenture
IRF	-	Industrial Rationalization Fund
KDB	-	Korea Development Bank
KDFC	-	Korea Development Finance Company
KECO	-	Korea Electric Company
KfW	-	Kreditanstalt fur Wiederaufbau
KFX	-	Korea Foreign Exchange
KIST	-	Korea Institute of Science and Technology
KLTCB	-	Korea Long Term Credit Bank
MCI	-	Ministry of Commerce and Industry
MOF	-	Ministry of Finance
NIF	-	National Investment Fund
POSCO	-	Pohang Iron and Steel Company
SMI	-	Small and Medium Industry
SMIB	-	Small and Medium Industry Bank
SSI	-	Small Scale Industry
TDF	-	Tourism Development Fund
TSD	-	Time and Savings Deposits

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## 1. THE INDUSTRIAL SECTOR

### Contribution to the Economy

1.01 Since the early 1960s, the industrial sector, and more specifically manufacturing, <sup>/1</sup> has been the engine of growth of the Korean economy. Over the period 1974-78, the manufacturing sector has grown at an average of 17.5% p.a. in real terms compared to an average 11% growth of aggregate GNP. In 1979, the growth rate of the manufacturing sector slowed to 10.6%, still higher than the 7.1% growth of real GNP. The share of manufacturing in total GNP has increased from 25.2% in 1974 to 32.7% in 1979. In 1975, for the first time the share of manufacturing in total real GNP exceeded that of agriculture; by 1979, agriculture accounted for only 18.8% of GNP compared to 32.7% for manufacturing. In 1979, seasonally adjusted manufacturing employment reached 3.1 million <sup>/2</sup> and accounted for 22.9% of the total employed population compared to 15.9% in 1973. Over the five-year period 1975-79, approximately 1.1 million jobs have been created in the manufacturing sector; this represented 53.6% of total net employment creation during that period.

1.02 Export Orientation and Export Dependence. Korea's success in economic development is largely based on a strategy of export promotion with emphasis on manufactured exports. Total commodity exports just exceeded US\$10 billion in current prices in 1977 but reached US\$15.1 billion in 1979. The volume of Korea's exports doubled between 1975 and 1978. The growth rate of commodity exports slowed in real terms to about 15.8% p.a. over the period 1977-78 compared to an average of 32.7% p.a. over the period 1972-76. In 1979, the nominal value of exports reached \$15.1 billion, 18.4% higher than in 1978; in real volume terms, however, this represented a 0.9% decline over 1978.

1.03 Manufactured products, which accounted for about 52% of total exports in 1964, have gradually increased their share and have remained at about 90% since 1976. Gradual changes have taken place in the structure of manufactured exports over the past three years: light manufactured products including textiles have declined in relative terms from 52.7% of total exports in 1977 to 50.4% in 1979; heavy industry products have increased their share from 32.8% in 1977 to 38.6% in 1979. However, some of Korea's traditional light exports such as footwear and clothing have remained buoyant. The changing composition of Korean exports reflects the significant changes which have taken place in recent years in the structure of the manufacturing sector.

1.04 It is estimated that export expansion contributed about 35% of the growth in manufacturing output over the period 1975-77 against 74% for

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<sup>/1</sup> In 1979, manufacturing alone accounted for 96% (in 1975 prices) of total value added in the industrial sector (i.e. mining and manufacturing).

<sup>/2</sup> Compared to 4.9 million in agriculture.

domestic demand./1 The real growth rate of the manufacturing sector was higher than that of exports in both 1978 and 1979, which, to some extent, reflects the growing demand for manufactured goods in the domestic market. Domestic demand has been expanding very rapidly in the past few years as a result of sharply rising incomes. A major investment boom, particularly in housing and manufacturing, started in 1977 and was an important element of the growing domestic demand. Excessive demand in the domestic market relative to the supply of goods increased inflationary pressures in 1978-79 and encouraged domestic sales in preference to exports. The erosion of the competitiveness of Korea's exports resulting from inflationary pressures coupled with a weakness in external demand contributed to a substantial deficit in the 1979 balance of payments. In the long run, however, rising domestic demand may prove a favorable development considering that, until 1977, the export dependence of the manufacturing sector had been growing faster than planned. The ratio of manufactured exports to output reached 26.9% in 1977 with considerable variations in the dependence ratio of the various subsectors./2

#### Structural Changes in Manufacturing

1.05 The growth of the manufacturing sector has been accompanied by significant adjustments in the importance of the various component subsectors as shown in the following table:

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/1 Import substitution made a negative (-9%) contribution.

/2 The export output ratio reached a level of 67% for wood and furniture and 91% for some miscellaneous products in 1977.

COMPOSITION OF VALUE ADDED IN MANUFACTURING, 1970-78  
(W billion in 1975 prices)

	1970		1974		1978	
	Amount	%	Amount	%	Amount	%
<u>Light Industries</u>						
Textiles	176.9	15.6	425.0	18.5	710.1	16.3
Others	484.0	42.6	798.9	34.7	1,336.3	30.7
Subtotal	<u>660.9</u>	<u>58.2</u>	<u>1,223.9</u>	<u>53.2</u>	<u>2,046.4</u>	<u>47.0</u>
<u>Heavy Industries</u>						
Basic metals	26.9	2.4	102.1	4.4	224.9	5.2
Machinery /a	111.1	9.8	361.0	15.7	971.2	22.3
Chemicals /b	336.7	29.6	614.1	26.7	1,107.4	22.5
Subtotal	<u>474.7</u>	<u>41.8</u>	<u>1,077.2</u>	<u>46.8</u>	<u>2,303.5</u>	<u>53.0</u>
Total Manufacturing	<u>1,135.6</u>	<u>100.0</u>	<u>2,301.1</u>	<u>100.0</u>	<u>4,349.9</u>	<u>100.0</u>

/a Including fabricated metal products.

/b Including paper and paper products, petroleum and nonmetallic mineral products.

Source: Table 8.13. World Bank Economic Report dated May 15, 1979.

1.06 The composition of manufacturing shows a marked shift in favor of heavy industry whose share of total manufacturing value added exceeded 50% for the first time in 1978. The most significant gains have been registered by the machinery sector. The rate of growth of chemical industries, however, lagged behind so that the sector declined from about 30% in 1970 to 22.5% in 1978. Light industries have declined steadily since 1970. The sharpest declines were recorded in the food, beverage and tobacco sector. Textiles have been maintaining their 16-17% share of total manufacturing value added. The changes in the structure of manufacturing reflect a deliberate policy to shift production gradually from Korea's traditional light industrial production towards more skill- and technology-intensive types of production.

Geographic Distribution

1.07 The 1975 population census showed that approximately 27% of the population of Korea lived in the cities of Seoul and Busan; the province of North Gyeongsang in which Taegu, the third largest industrial city is located,

accounted for another 14%. The following table shows that the regional distribution of manufacturing enterprises and employment is skewed in favor of Seoul and Busan.

GEOGRAPHIC DISTRIBUTION OF INDUSTRY  
(%)

	1974			1977		
	No. of enterprises	No. of workers	Value added	No. of enterprises	No. of workers	Value added
Seoul and Busan	34.6	48.7	44.5	38.6	46.2	37.5
Other regions	665.4	51.3	55.5	61.4	53.8	60.5
<u>Total</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: Report on Mining and Manufacturing Survey. EPB 1977.

While Seoul and Busan remain the largest industrial centers, marginal improvements have taken place between 1974 and 1977 in the redistribution of industrial employment outside these areas. This may be the first sign that government policies aimed at a better distribution of employment are having an impact. Government policies aiming at reducing the congestion of Seoul and Busan include severe restrictions on industrial expansion in these two cities, a program of financial assistance for the relocation of industries, the promotion of new industrial estates such as the Pohang, Ulsan and Yeosu complexes and the Saemaeul Movement, initiated in 1971, for creating off-farm employment in rural areas.

#### Factor Use and Efficiency

1.08 The main elements which have contributed to the rapid expansion of the manufacturing sector are (a) a high rate of investment and (b) efficiency in factor use, both capital and labor.

1.09 Gross Fixed Capital Formation. Real fixed investment increased sharply by an average of 33% p.a. over the two-year period 1977-78 and slowed down to 9.6% in 1979. As a result, the ratio of gross fixed capital formation to GNP rose in real terms from 25.9% in 1976 to 37.1% in 1978 and edged up further in 1979 to 38%. Housing and manufacturing were the leading investment sectors. Manufacturing investment increased by a phenomenal 63.4% in real terms in 1978 and a further 17.4% in 1979. As a share of total fixed investment, manufacturing reached 38% in 1979 compared to an average of 21.9% over the period 1975-77. Within manufacturing, a major part of investment was directed towards fulfilling ambitious government targets for heavy industry. Heavy industry accounted for 78.9% of total manufacturing investment in



1977-79. Investment in light industry accounted for the remaining 21.1% and lagged significantly behind the Fourth Plan targets. Investment in heavy industrial projects with long gestation periods did not lead to an immediate increase of productive capacity and contributed to aggravating the imbalance between domestic demand and supply. Indications are also that investment in heavy industries has exceeded in some instances the levels dictated by market size, financing capacity and technical capability. Overinvestment is already apparent in certain branches of industry. In view of these structural problems and of the overheating of the economy to which investment in some heavy industries contributed, the Government has taken steps to delay, scale down or cancel several investment projects. An Investment Project Coordinating Committee was set up in 1979 to review investment priorities and projects and to pursue rationalization steps.

1.10 Factor Efficiency. Efficiency in factor use has contributed to the high performance of the Korean manufacturing sector. Calculations of incremental capital to output ratios (ICORs) with a one-year lag show a gradual decline over the three consecutive periods 1961-66, 1966-71 and 1971-75, indicating increasing efficiency in the use of capital investment. Inclusion of data for 1976 and 1977 raises the ICOR estimate to 1.012/1 for the period 1971-77 compared to 0.977 /1 for the period 1971-75. This may reflect the higher capital intensity of manufacturing investment in recent years because of the larger share of the heavy and chemical sectors. Efficiency in capital utilization is also evidenced by the rapid growth in industrial capacity utilization over 1971-77; over the past two years, however, excess capacity has appeared in some branches of industry. Labor productivity measured by the ratio of value added per employee has also been increasing in all manufacturing subsectors over the period 1970-76 and was sufficient to absorb wage increases. Over the period 1977-79, however, productivity gains have lagged behind the rapid growth in real wages. Rising labor costs have contributed to the decline in the competitiveness of Korean exports in 1978-79.

#### Financial Structure of Enterprises

1.11 The tight controls exercised by the Government on credit allocation by financial institutions have enabled the direction of investment patterns according to national priorities. The system of preferential credits has also encouraged excessive credit demand and has resulted in the very high indebtedness of manufacturing enterprises. The average aggregate debt/equity ratio of manufacturing enterprises which stood at 2.7:1 in 1973 following the financial measures of 1972, has increased steadily and reached 3.7:1 in 1978. The long-term debt/equity ratio, however, reached only 1.5:1 in 1978, reflecting an excessively large share (58%) of short-term borrowings in total debt. The 1979-80 economic recession has induced greater reliance on short-term borrowings to finance inventory build-up. The average aggregate debt/equity ratio of manufacturing enterprises is now estimated at about 4:1. The average interest rate paid on borrowings, short- and long-term, ranged from 12% to 13% over the period 1976-78. Profitability measured in terms of net income to total assets has declined marginally from 3.2% in 1976 to 2.7% in 1978 but remained satisfactory.

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/1 Based on 1970 constant prices.

## Industrial Policies

1.12 The phenomenal growth of the manufacturing sector was, to a large extent, made possible by efficient and pragmatic government policies. Incentive packages have been developed and adjusted over time to fit evolving priorities for industrial development. With variable emphasis, policies have aimed at the promotion of export industries, import substitution, assistance to small and medium enterprises, geographic dispersal of industry and in the last few years, promotion of skill-intensive sectors with a higher technological content. Export promotion has been the major objective since the early sixties. Subsidies on exports have continued to increase in absolute terms over the period 1975-78 but were insufficient to compensate for the loss of competitiveness induced by Korea's higher prices relative to its major trading partners. As a result, the real effective exchange rate deteriorated sharply for Korean exporters over that period.

1.13 Export Incentive System. Government incentives to exporting industries include tax exemption, accelerated depreciation allowances, refund of import duties on raw materials used for export production, deferred payment of tariffs on equipment and access to subsidized credit. These incentives are administered within the framework of an export targeting system whereby exporting firms set for themselves certain export targets in agreement with overall government objectives. A monthly conference is held to review and adjust targets as well as government policies affecting their implementation.

1.14 While the emphasis has clearly been on export promotion, key import substitution industries have received substantial government support in the form of partial tax and tariff exemptions, as well as protection from competing imports. Production for the domestic market, however, has generally been subject to higher duties, taxes, and interest charges on borrowings. In 1977-78, the Government relaxed a number of import restrictions as part of an import liberalization program to be implemented over a four-year period. Banned items have been abolished; since January 1, 1979, 69% of all import items are subject to automatic approval, 31% are "restricted".<sup>/1</sup> Tariff adjustments have also been introduced to improve the competitiveness of import substituting industries. The simple average tariff rate has been reduced from 36% to 25%.

## Recent Performance

1.15 The rapid growth of the Korean economy during 1977-78 was followed by a recession in 1979. Real GNP growth rate slowed in 1979 to 6.4%, compared to an average of 10.9% p.a. over the period 1977-78. Exports stagnated and a large deficit of \$4.2 billion was recorded in the current account of the balance of payments. Over-expansion of the economy in the period 1976-78 linked with international recession and protectionism may be the root cause of

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<sup>/1</sup> In early 1978, 54% of all items were subject to automatic approval, 41% were restricted and 5% were banned.

the lackluster performance of 1979. The overheating of the economy resulted from expanding incomes and excessive domestic demand, particularly investment demand. In order to quell inflationary pressures, the Government implemented in 1978-79 an import liberalization and stabilization program which included tight monetary and fiscal policies. The resulting slowdown of the economy was sharper than expected because of the continued stagnation of exports and high level of inflation. Further economic adjustments were made in January 1980: the Won was devalued by 16.4% relative to the US dollar, interest rates were raised by 6 percentage points and domestic energy prices increased dramatically.

1.16 The industrial sector provided the major impetus to GNP growth over the period 1977-79. The growth of the manufacturing sector reached an average of 17.5% in real terms over the period 1977-78 but slowed down to 10.6% in 1979. Industry was hard hit by cost-push inflation and by the economic recession of 1979. Seasonally adjusted industrial output in the final quarter of 1979 was 4% below the first quarter level. Tightness in the labor market pushed up unit labor costs by over 20% p.a. during 1977-79 and real wages by 16% p.a. Real wage increases have substantially outstripped productivity gains in recent years and caused an erosion of Korea's comparative advantage in the labor-intensive manufactures which still dominate its exports.

#### Prospects

1.17 The latest Economic Management Plan of the Government estimates GNP growth rates of 3% and 7.5% in 1980 and 81 respectively. Over the same period, industrial sector growth rates are expected to be 2.8% and 9.1%. Overall investment is projected to decline by 8% in real terms in 1980.

1.18 In spite of the current difficulties, Korea's long-term growth potential remains favorable. Continued stimulation of exports at about 12% p.a. over 1980-81 is crucial for recovery in the economy. At the same time, some restructuring of the economy, particularly in the industrial sector, seems desirable to improve efficiency. Korea's shift from labor-intensive towards skill-intensive industries ought to be pursued but investments in heavy industry need to be carefully reviewed and rationalized to avoid overinvestment and excess productive capacity.

## 2. THE FINANCIAL SECTOR

2.01 The unparalleled expansion of Korean industry since the early 1960s was made possible by an ambitious investment program coupled with pragmatic financial sector policies. The financial system effectively supported the growth of industry by mobilizing the necessary foreign and domestic savings and by efficiently channeling these resources toward industrial investment. As a result, Korea's financial sector and institutions have expanded rapidly. From the outset, however, financial institutions and funding mechanisms have been kept under tight government control to ensure the allocation of resources

to predetermined priority areas. The system has worked well in the past decade; there is, however, some concern about its ability to respond efficiently and flexibly to the requirements of an increasingly complex and sophisticated economy.

#### Financing Gross Domestic Capital Formation

2.02 The rapid growth of manufacturing investment over the period 1977-79 was made possible by an equally rapid growth of long-term loans /1 extended by Korean financial institutions to the manufacturing sector. Manufacturing fixed investment increased by an average of 45% p.a. in current prices over 1977-79 and net term lending /2 by an average of 52% p.a. The rapid growth of debt financing suggests that financing patterns have remained substantially unchanged over the past three years and that Korean industries have kept a high level of indebtedness (para. 1.11). Recent Bank surveys of the financing of industry in Korea indicate that, on average, self-financing by Korean enterprises accounts for only 30% of investment /3 and the remainder is covered by borrowings. This financing pattern stems largely from the availability of debt financing at a low cost relative to other types of funding.

2.03 Current price fixed investment in manufacturing amounted to W 2,174 billion in 1979. Assuming that self-financing accounted for 30%, external debt financing provided the balance, namely W 1,522 billion. External finance was in the form of borrowings from domestic financial institutions and from noninstitutional sources (capital markets, borrowings from abroad and unorganized money market). In 1979, incremental term lending by Korean financial institutions to the manufacturing sector amounted to W 1,067 billion or 70% of the external financing estimated above. Noninstitutional sources provided the balance of W 455 billion, of which about half was generated through issuance of corporate debentures in the securities market and the other half from foreign commercial loans and suppliers' credits./4

2.04 The above figures indicate that approximately 50% of manufacturing fixed investment in 1979 was financed by Korean financial institutions, while self-financing accounted for 30% and noninstitutional sources for the remaining 20%. The relative importance of the various Korean financial

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/1 Defined as loans with a maturity exceeding one year.

/2 Defined as the increase in term loans outstanding.

/3 20% through retained earnings and 10% by additional equity investment.

/4 This breakdown is highly tentative and based on the assumption that long-term fixed investment is financed out of long-term resources; in fact, the high short-term indebtedness of Korean industry suggests that short-term debt is used in part to finance fixed assets and rolled over.

institutions in supplying long-term funds (defined as loans with a maturity exceeding one year) for industry is shown in the following table:

INCREMENT IN OUTSTANDING TERM LOANS TO MANUFACTURING BETWEEN 1977 AND 1979  
(In W billion)

	Amount	%
Commercial banks	530.2	27.4
Korea Development Bank	613.3	31.7
Korea Development Finance Corporation	113.1	5.8
Small & Medium Industry Bank	152.9	7.9
Citizens National Bank	11.8	0.6
Korea Exchange Bank	303.4	15.7
Export Import Bank	155.1	8.0
Life insurance companies	54.2	2.8
Insurance companies	3.7	0.2
<u>Total</u>	<u>1,937.7</u>	<u>100.0</u>

The Korea Development Bank (KDB) is the single largest source of term finance for industry. Commercial banks come next, having in certain years provided in aggregate more funding with a maturity exceeding one year than KDB. However, term lending by the commercial banks is usually for working capital rather than equipment financing and for shorter maturities than KDB's (four to five years on average compared to eight years for KDB). The General Banking Act limits the maturity of commercial bank term lending to ten years. The Korea Exchange Bank has also become an important source of term finance for export industries. The Korea Development Finance Corporation (KDFC), however, has seen its contribution gradually erode from 14% in 1974 down to 4% in 1979 (Annex A, Table 1).

2.05 While commercial banks are an important source of funding with a maturity exceeding one year for industry, their main activity is the supply of short- and medium-term working capital funds. In fact, term lending by commercial banks has remained through the 1970s well below the potential afforded by available term resources such as time and savings deposits (TSD) and equity. Extensive rollover of short-term loans *de facto* increases term lending but is somewhat less suitable for financing fixed investment. Incremental short-term loans of commercial banks to manufacturing reached W 2,761 billion in the period 1977-79 compared to W 530.2 billion for long-term loans. Looking at the aggregate short- and long-term resources flowing to industry over 1977-79, commercial banks accounted for 60%; KDB was the next largest supplier with 14.8% (Annex A, Table 2).

### Institutional Sources of Funds

2.06 The institutional set-up of the Korean financial sector can be divided into (a) banking (or monetary) institutions which accept deposits from the general public and (b) nonbank financial institutions. Banking institutions <sup>/1</sup> comprise conventional commercial banks, including branches of foreign banks, and six specialized banks.<sup>/2</sup> The operations of commercial banks are directly supervised by the Bank of Korea (BOK) while specialized banks are under the control of the Ministry of Finance (MOF).

2.07 Annex A Table 3 shows the assets structure of the Korean financial system. Over the period 1975-79, some deepening of the financial sector has taken place as reflected by the growing importance of nonbank institutions. The share of nonbank financial institutions in the total gross assets of the financial sector reached 26.2% in 1979 compared to 23% in 1975. This sign of maturity notwithstanding, the banking system including BOK still accounted for 73.8% of the sector's total assets in 1979; BOK and the commercial banks together accounted for 51% of total financial sector assets.

2.08 The Commercial Banks. The commercial banking sector in Korea comprises: (a) five government controlled commercial banks with a nationwide network of branches; (b) ten private banks with operations localized in each province; and (c) branches of foreign commercial banks. Commercial banks are subject to the provisions of the General Banking Act. In aggregate, the assets of commercial banks accounted for 38.9% of the total assets of the financial sector in 1979, up from 37.7% in 1975; the 1979 component ratio of 38.9% could be broken down into 31.5% for the five nationwide banks, 4.1% for the ten regional banks and 3.3% for branches of foreign banks. The commercial banking group remains by far the largest source of funds for the manufacturing sector, but its importance has been slowly declining over time in relative terms. The commercial banks accounted for 54.7% of the increase in outstanding loans to the manufacturing sector in 1979 compared to 73% in 1974. Their operations, however, are heavily skewed towards short-term lending, in part, because they lack the expertise required to carry out the appraisal of long-term investment proposals. In 1977, short-term loans accounted for approximately 97% of the increase in the total commercial banks portfolio; in 1979, the ratio was still as high as 70%.

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<sup>/1</sup> Also referred to as "deposit money banks" (DMBs).

<sup>/2</sup> The Korean Exchange Bank for foreign trade; the Small and Medium Industry Bank for SMI; the Citizens National Bank for consumer finance and SSI; the Korea Housing Bank for housing finance; the National Agricultural Cooperative Federation for agricultural credits and the National Fisheries Cooperative.

2.09 Deposits represent the major source of funds of commercial banks. In 1978, demand and savings deposits together accounted for 54.3% of total aggregate liabilities (including equity). This ratio was substantially lower than the 71.1% reached in 1970. Demand deposits had marginally increased their share of total resources to 21.4% in 1978, but time and savings deposits had declined steadily from 52.4% in 1970 to 32.9% (Annex A, Table 4). This sharp decline could be related to the 1972 reduction in interest rates and the negative real deposit rates which resulted.

2.10 Specialized Banks. The six specialized banks were created by the Government in the 1960s to service particular economic sectors. The specialized banks were established under separate legislation. They are not subject to the General Banking Act and lie outside the jurisdiction of the Central Bank's regulations. Their operations are supervised directly by MOF. Their aggregate assets accounted for 22.6% of the total assets of the financial sector in 1979, down from 23.6% in 1975. The Korea Exchange Bank, which was established in 1967 to take over the commercial foreign exchange transactions of BOK, accounts for more than half the total assets of specialized banks. Demand and savings deposits represent the main source of funds of specialized banks; they accounted for 58% of total liabilities /1 and equity at end-1979.

2.11 Nonbank Financial Institutions. The declining share of the monetary system, i.e., specialized banks, commercial banks, and BOK /2 in the total assets of the financial sector reflects a certain deepening of the financial system and the growing importance of nonbank financial intermediaries. The average annual growth rate of the assets of nonbank financial institutions, reached 17.2% in real terms over the period 1975-79 compared to an average of 13.7% for the financial sector as a whole. Their share of total assets consequently increased from 23.2% in 1975 to 26.2% in 1979. Nonbank financial intermediaries comprise: (a) four development banks /3; (b) the trust account of the Bank of Seoul and Trust; (c) life and nonlife insurance companies; (d) short-term finance companies (STFC); (e) mutual savings and finance companies; (f) postal savings accounts; and (g) securities firms. Of the seven types of nonbank intermediaries, development banks constitute the largest group, accounting for 59% of the total assets of nonbank financial intermediaries in 1979.

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/1 Excluding guarantees issued and outstanding.

/2 BOK's share of financial sector assets declined from 15.5% in 1975 to 12.4% in 1979.

/3 The Korea Development Bank; the Korea Development Finance Corporation; the Korea Export-Import Bank; and the Korea Land Development Corporation, formerly the Land Bank.

2.12 The Bank Group is associated with the two development banks which are active in the industrial sector: KDB and the KDFC.<sup>/1</sup> The Government-owned KDB is the largest financial institution in Korea. As the principal agent of government long-term funding programs, it deals primarily with large public and private sector enterprises in power, transportation and manufacturing. The privately owned KDFC also finances relatively large industrial enterprises but only in the private sector.

#### Noninstitutional Sources of Funds

2.13 Noninstitutional sources of funds include (a) the unorganized money market (UMM) which is primarily a source of short-term resources; (b) direct corporate borrowings from outside Korea; and (c) the Korean capital market. Estimates of the importance of the UMM are made difficult by the very nature of the transactions undertaken and by the fact that a substantial part of the lending operations of STFCs actually utilize "recycled" UMM resources. Among foreign sources of funds, medium-term suppliers' and buyers' credits provide substantial resources for Korean industries (Annex A, Table 5). These direct borrowings from abroad are classified as a noninstitutional source of funds but their availability is usually dependent upon a counterguarantee from a local financial institution.

2.14 Other noninstitutional sources of funds comprise direct foreign equity investments and the securities market. Direct foreign investments are restricted by the Government to specific sectors; they amounted to US\$124 million in 1979. The stock and bond markets, particularly the latter, have developed over the past few years into important sources of finance for the manufacturing sector. The importance of the stock market as a source of term finance has fluctuated during the 1970s. Stock market activity expanded rapidly through the mid-70s as a result of government incentives to induce firms to go public. The main incentive was in the form of a 13% tax differential between closed and listed firms. This differential has been reduced to 5% in 1978. New listings increased by 10% only in 1978 and the number of listed companies actually declined to 355 in 1979. Trading also declined and the stock price index plummeted from 207.2 at end-1978 to 169.1 at end-1979. Funds raised by manufacturing enterprises on the stock market amounted to W 141.1 billion in 1978 and W 107.3 billion in 1979.

2.15 Since 1977, the corporate bond market has been supplying more resources <sup>/2</sup> to the manufacturing sector than the stock market. The value of new bond issues has been increasing at an average of 80% p.a. over 1977-79.

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<sup>/1</sup> The Bank has also made three loans to SMIB and a first loan to CNB in 1980. Both institutions are considered as deposit money banks because they accept deposits from the general public. However, a substantial part of their operations is, in fact, development financing.

<sup>/2</sup> On the basis of gross offerings; no information is available on redemptions.



New offerings reached W 465.2 billion in 1979. The effective yield of corporate bonds varies from 33.5% to 36.6% p.a. for a 2-year maturity following the January 1980 reform of the interest rate structure. The rapid growth of the bond market is, to a large extent, due to the favorable tax treatment granted to bond buyers.

#### Government Control and Direction

2.16 The development of Korea's economy over the past 20 years has been directed by comprehensive governmental planning designed to influence private sector decisions and to provide the means, including finance, for their implementation. Strict control over the financial system has thus been viewed by the Government as an efficient tool for enforcing tactical decisions within the economic development strategy. The operations of the financial sector are characterized by close government controls on the day-to-day management of the institutions, on their funding and on their allocative function. The Government directly owns controlling participations in the share capital of four of the five nationwide commercial banks and indirectly controls the fifth one. The Government also has majority holdings in the six specialized banks and is in full control of the Korea Development Bank and the Export-Import Bank. The top management of these institutions is usually appointed directly by the highest authority on the basis of recommendations by the Minister of Finance. Altogether, the BOK, the five commercial banks, the six specialized banks, KDB and Exim Bank account for more than 80% of the assets of the financial system. KDFC is the only major development institution which is wholly privately owned.

2.17 Government controls on fund mobilization by the financial sector are exercised in various ways: (a) the Government is the main participant in the share capital increases of commercial and specialized banks; (b) the Government supplements DMB and KDB resources with funds earmarked from the budget and from special funding programs such as the National Investment Fund (NIF);<sup>/2</sup> (c) BOK has opened rediscounting facilities for DMBs, the main one being short-term export credits; and (d) the Government administers interest rates on deposits and other instruments of mobilization such as bonds and debentures. The administrative controls extend beyond government-owned institutions as nonbank financial institutions such as KDFC and the short-term finance companies are expected to "follow" the interest rates set for DMBs. Numerous controls also exist on the operations of the securities market.

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<sup>/1</sup> On the basis of gross offerings; no information is available on redemptions.

<sup>/2</sup> Annex C provides a detailed description of the NIF program; para. 2.22 gives a summarized analysis.

2.18 Directed Credit. Government controls are pervasive in the area of fund allocation. The administrative guidelines on "Uses of Funds in the Financial Sector" issued by the Monetary Board in 1958 have increasingly been replaced by specific directives to DMBs and KDB regarding not only the allocation of government funds but also the allocation of their own resources to specific priority sectors, subsectors and sometimes individual projects or firms. The system of directed lending which is administered by BOK and MOF provides financing at government behest to recognized prime borrowers and, therefore, severely limits the discretion exercised by financial institutions in fund allocation. The proportion of Government-directed lending has been estimated at about 40% of total DMB lending./1

2.19 Subsidized Credit. An important feature of directed credits is the low interest rate charged on most of the loans, a notable exception being the small industry loans of commercial banks. At least half of the directed loans of DMBs are at concessional rates (i.e., below the normal rate for nonpriority borrowers)./2 Export credits and the NIF program are the main components of subsidized lending by the DMBs and KDB. A rising share of DMB subsidized lending (from 40% in 1971 to 56% in 1978) is for short-term export financing. NIF lending had also increased from 9% of DMB subsidized lending in 1975 to 20% in 1977 (Annex A, Table 6). NIF loans accounted for 38% of KDB's loan portfolio at end-1979 up from 29% at end-1977.

2.20 Export financing is given the highest priority by the Government because export growth is crucial to the Korean economy. The availability of concessional loans for exports is viewed as equalizing the position of Korean exporters with international competitors. These loans are channelled through the commercial banks and can be rediscounted with BOK for 80% of their value. Handling banks receive an interest spread of 5 percentage points. The final lending rate of 9% p.a. was raised to 12% in January 1980 and will increase to 15% p.a. by end-1980. By comparison, the prime lending rate for short-term loans was raised to 24.5% p.a. in January 1980.

2.21 Operation of the NIF started in 1974 (Annex C). Total NIF loans outstanding reached W 1,228 billion (\$2.5 billion) at end-1979. Contributions by banking institutions out of their deposit resources supply approximately 75% of total NIF funding. NIF loans are available primarily for financing equipment purchases with a maximum maturity of 8 years. The NIF program aims at supporting the restructuring of the industrial sector and therefore places emphasis on assistance to heavy and chemical industries. The commercial banks, the specialized banks and KDB allocate NIF loans; at end-1979 they accounted respectively for 18.2%, 15.9% and 65.9% of outstanding NIF loans. Final lending rates were raised in January 1980 to 21-22% compared to a nonconcessional rate for term loans of 24.5-25.5%. Handling banks

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/1 On an outstanding basis over 1977-78.

/2 Representing about 20% of total outstanding loans.

operate with a positive spread of 0.5% to 1.5%; the interest rate subsidy is absorbed by the Government.

#### Efficacy of the Control System

2.22 The efficacy of government controls over the financial system must be judged in terms of (a) impact on financial intermediation; (b) efficiency of resource allocation by institutions; and (c) internal efficiency of intermediaries. These three elements are obviously interrelated.

2.23 Financial intermediation is dependent upon the mobilization of sufficient savings. The ratio of aggregate savings to GNP exceeded 25% through most of the period 1970-79, reaching 35% in 1979. Korea's savings performance has been high by most international standards. The ratio of time and savings deposits to GNP, however, dropped from 23.3% in 1973 to 21.3% in 1974-79. Equity resources and term deposits are the main source of term funding for the commercial and specialized banks. The slow growth of TSD, therefore, affected the capability of these institutions to function as efficient financial intermediaries. TSD interest rates are determined by the Government and have, in real terms, been close to zero or negative since 1972. Low interest rates on financial instruments have caused some financial disintermediation in the household sector whereby household savings have been diverted from deposits into real estate acquisition. The January 1980 upward adjustment of interest rates partly remedied this situation and was followed by a sharp increase in aggregate TSD. Another element of government control on financial intermediation has been the push toward lengthening the maturities of loans by Deposit-Money Banks to expand capital formation. As a result, term lending by commercial banks has increased in absolute and relative terms through the 1970s but has apparently failed to reach the potential afforded by available term resources.

2.24 The allocational efficiency of the system of directed lending has been satisfactory in terms of aggregate flow of funds toward the priority areas of export and heavy industry. It appears, however, that the magnitude of interest subsidies has resulted in excess demand for debt financing and may have led to some misallocation of funds within the too broadly defined priority areas. Favored access to financing for ill-defined priority borrowers may have led to suboptimal investment decisions with respect to product choice, scale of production and capital intensity. Excessive credit expansion has also fueled inflation and has encouraged a high level of indebtedness in the corporate sector. The high indebtedness of Korean industry appears to be worrisome owing particularly to the high proportion of short term debt resulting from easy access to cheap export credits.

2.25 The combination of excess loan demand and government-directed lending has had a detrimental impact on the internal efficiency of intermediaries. The ability of banks to undertake adequate appraisals and to exercise proper business judgment has been restricted. Competition among financial institutions has been severely limited. As a consequence, the transaction

costs of commercial banks are high and bad loans are reportedly kept at an artificially low level through reschedulings, refinancing of arrears and rollover of debt.

2.26 Critics of the operations of the Korean financial sector recognize that the system has, in the past, contributed to the phenomenal growth and transformation of the industrial sector in accordance with national priorities. On the other hand, the system was responsible for excessive credit expansion and inflation. Directed lending also has encouraged high debt/equity ratios in the corporate sector and has contributed to excessive investment in some branches of heavy industry. Doubt has been expressed by the Korean authorities themselves about the desirability of maintaining the rigid system of centrally directed lending because of the growing complexity of the economy. The need for fine tuning of investment decisions cannot be flexibly accommodated under the present system. It is recognized that directed and concessional lending should not be discontinued but should be reduced in scope and size to clearly defined priority sectors and branches of industry. At the same time, some liberalization of the operations of the financial sector, particularly of commercial banks, seems desirable and timely.

#### Reform of Financial System

2.27 Bank surveys of the Korean financial system have led to a number of specific recommendations aimed at improving the efficiency of the financial sector. The main recommendations are summarized below:

- (a) interest rates on time/savings deposits and lending rates should be maintained at a positive level in real terms to encourage a reliable flow of term resources into the DMBs;
- (b) the proportion of directed lending made for specified purposes and borrowers at government behest should be reduced relative to total lending;
- (c) the share of directed lending which commands concessional interest rates, primarily export credits and NIF, should be reduced in scope and volume and the extent of the interest subsidy ought to be reassessed;
- (d) as directed concessional lending is reduced, institutional arrangements for delivery of funds, particularly NIF, ought to be rationalized. Concentration of NIF lending in the specialized banks and KDB is recommended since these institutions have the necessary expertise in term lending. Commercial banks would be freed to meet other credit needs including export financing;
- (e) more operational discretion in management and operational decisions should be given to the commercial banks to increase efficiency and competition;

- (f) harmonization of foreign currency lending rates and interest spreads ought to be improved;
- (g) monetary and credit control instruments available to the BOK ought to be broadened and made more flexible; and
- (h) the bill market, securities market and housing finance ought to be further developed and encouraged through a comprehensive set of incentives.

2.28 The Government is aware of the shortcomings and inefficiencies of the Korean financial system. A policy dialogue between the Bank and the Government on these matters has been initiated and will be pursued. Interest rates have already been raised in January 1980 with the intention of maintaining real rates at a positive level. A move towards liberalization of the sector has also been announced which, over time, would provide greater autonomy to financial institutions. As a first step in this direction, the Long-Term Credit Bank Law was enacted in November 1979. The purpose of this legislation is to encourage the establishment of a new type of financial intermediaries operating outside the Government's system of directed lending. Long-term credit banks would be privately-owned institutions raising a major part of their resources from the domestic capital market and focusing on long-term lending for industry. In June 1980, KDFC changed its legal status and became Korea's first long-term credit bank.

#### Lending Rates and Inflation

2.29 The continuing high rate of inflation has been a serious problem in Korea for the past two decades. High inflation has led to a worsening of Korea's terms of trade and to a loss of real income in relation to real production. Despite recessionary tendencies in 1979, wholesale and consumer prices rose by over 18% during the year compared to 12-14% during 1978. Following the January devaluation of the Won and the dramatic increase in domestic energy prices, inflation worsened in early 1980. In the first quarter of the year, the consumer price index increased by 12.1% and the wholesale price index by 22.2%. Annual increases in the consumer price index have been projected at 25.4% and 14.8%, respectively, for 1980 and 1981; actual increases may be higher.

2.30 Domestic Currency Lending Rates. The January 1980 upward revision of the interest rate structure (Annex A, Table 8) brought nonconcessional lending rates for prime borrowers to 24.5% p.a. for working capital and 26.5% for equipment loans with maturities exceeding eight years.<sup>/1</sup> While the adjustment of domestic currency interest rates to a positive level in real terms is a step in the right direction, additional adjustments seem justified with respect to foreign currency lending rates.

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<sup>/1</sup> Working capital loans to nonprime borrowers carry a 25% lending rate and equipment loans a rate of 25.5% for 3-8 years and 24.5% under 3 years.

2.31 Foreign Commercial Borrowings. Until June 1980, the lending rate for foreign currency loans funded with Eurodollar commercial borrowings was fixed by MOF at LIBOR + 1% to LIBOR + 1.25% depending on maturity. KDFC was authorized to charge a slightly higher rate of LIBOR + 2%. With six-month Eurodollar rates currently at about 14 % p.a. (down from 20% in April 1980) a spread of 1.25% over LIBOR was equivalent to a 15.25% p.a. charge on a dollar-denominated loan. Over the ten-year period 1971-80, the average annual depreciation of the Won vis-a-vis the US dollar was about 6% p.a. In Won terms, a Eurodollar borrowing therefore carried an interest rate of about 21.25% p.a. for the final borrower, compared to the normal rate of 26.5% p.a. on Won borrowings. Admittedly, the same computation in April showed a cost of about 27.25% p.a.; it seems, however, that on average, over a period of several years, access to foreign commercial funds did provide an element of subsidy to the borrower. Given this context, there was little rationale for keeping the interest spread accruing to the financial intermediaries at about 0.5% /1 which was much lower than the 2% spread allowed on foreign borrowings from official sources and was insufficient to cover handling costs. The lower interest spread on foreign commercial borrowings effectively represented a disincentive to more mobilization of resources. In June 1980, an interest spread of about 2% was authorized by the Government as a means of reducing the subsidy to the final borrower and lessening the reliance of financial intermediaries on official sources of funds.

2.32 Foreign Official Borrowings. The effective cost to subborrowers of foreign resources raised from official agencies such as IBRD and ADB is more difficult to estimate in Won terms because of the variable currency mix of disbursements. KDFC has carried out a detailed analysis of the cost of funds under three of the loans it received from the Bank. Under Loan 1145-KO the nominal borrowing rate from the Bank was 8.5%. In accordance with the standard practice imposed by the MOF, funds were onlent with an interest spread of 2% and the foreign exchange risk passed on to the subborrowers. The nominal onlending rate therefore stood at 10.5% p.a. Disbursements of "hard" currencies (Yen, Deutsche Mark and Swiss Francs) which appreciated against the US dollar reached 61% of total disbursements. As a consequence, the effective rate, in dollar terms, for the subborrowers reached 19.5% p.a./1 The average appreciation of the US dollar vis-a-vis the Won reached about 7% p.a. over the loan disbursement period, thus bringing the effective lending rate in Won terms to 26.5% p.a./2 By comparison, KDFC's standard lending rate for domestic currency equipment loans stood at 20.5% p.a. until January 1980 and has since been raised to 26% p.a. Other official loans to KDFC and other financial intermediaries in Korea, including KDB, had a similar effective cost and therefore do not appear to impart any sizeable interest subsidy to the recipients by comparison with Won-denominated loans and with foreign commercial loans.

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/1 Assuming a borrowing cost for the intermediary of LIBOR + 0.75% and an onlending rate of LIBOR + 1.25%. KDFC has been allowed a margin of 1.25%.

2.33 Onlending practices for foreign official borrowings, however, do create some distortions in final lending rates due to the government policy of requiring that these loans be onlent with a uniform spread of 2%. With substantially different lending costs over time and between lending agencies, subborrowers from the same institution, at the same time, ostensibly similar in essential characteristics, obtain funds on different terms. It was agreed at negotiations that each financial institution would be allowed to commingle its official foreign resources and that a spread of 2% be applied to the weighted average cost of these funds.<sup>/3</sup> This results in a uniform onlending rate subject to adjustment as new lines of credit are mobilized from official sources.

#### Bank Lending Strategy

2.34 Bank lending to Korean industries is effected primarily through specialized long-term financial intermediaries. This type of lending was initiated 12 years ago with a first loan to the Korea Development Finance Corporation (KDFC). The Bank has now established a solid relationship with four Korean Development Finance Companies (DFCs) which, in aggregate, supplied over 50% of the increase in medium and long-term loans extended to the manufacturing sector in 1977-78. The Bank has helped meet the financial needs of medium and large-scale firms primarily through KDB and KDFC.<sup>/4</sup> The financial support of smaller-scale enterprises by the Bank was initiated in 1975 through a first loan to the Small and Medium Industry Bank (SMIB) and to the Citizens National Bank (CNB) in 1980.

2.35 The Strategic Role of KDB and KDFC. The long association of the Bank with KDB and KDFC has had a very positive impact in terms of (a) overall resource transfer to the vitally important industrial sector; (b) the building up of large and efficient development finance institutions; and (c) developmental impetus in the financial and industrial sectors.

2.36 KDB and KDFC through the complementary, though distinct nature of their operations occupy a central position in the financial sector and serve as the two major conduits of resource flows to the priority manufacturing sector. Over the period 1974-79, KDB and KDFC jointly supplied 37.5% of all term loans to the manufacturing sector. Bank financial support of KDB and KDFC's operations was instrumental in enabling the two institutions to assume an increasing role in the transfer of resources to the industrial sector.

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<sup>/1</sup> On average over the period 1976-80.

<sup>/2</sup> Similar calculations for earlier loans show an effective lending rate in Won terms of 18.5% for Loan 705-K0 and 17.4% for 905-K0.

<sup>/3</sup> Weighted by the amount of funds available for future lending.

<sup>/4</sup> Seven Bank loans aggregating \$320 million have been made to KDFC and three loans for a total of \$252.5 million to KDB.

2.37 The financial and technical support supplied to KDB and KDFC through the Bank's lending operations in the past few years has also had a substantial impact on their efficiency and quality as financial intermediaries. KDB and KDFC have gradually developed into the most efficient intermediaries on the Korean financial scene, and both now rank among the best DFCs with which the Bank is associated worldwide. This is reflected not only in the appropriateness of their operational procedures but also in the quality of their portfolio and in their success at mobilizing foreign currency resources from commercial sources.

2.38 Finally the Bank's support of KDB and KDFC has had an impact which extends beyond the two institutions to the industrial and financial sectors. The developmental role increasingly assumed by the two intermediaries has led to a more balanced sectoral and geographic distribution of industries in Korea and has helped to deepen the structure of the financial sector. Both KDB and KDFC have sponsored the establishment of several specialized financial institutions including leasing companies, investment banks, merchant banks and short-term finance companies as a means of increasing the range of financial services available in Korea.

2.39 Satisfactory as this performance and impact on the overall economy might be, an analysis of the operations and efficiency of both KDB and KDFC shows a number of shortcomings stemming, in part, from the financial environment in which they operate. The Bank now proposes to use its lending operations to KDB and KDFC as a vehicle for addressing with the Korean Government the general financial sector issues which affect the efficiency of individual institutions.

2.40 The recent Economic Report prepared by the Bank <sup>/1</sup> indicates that inefficiencies have surfaced in the structure and operations of the industrial sector in Korea and may have contributed to the lackluster performance of the Korean economy in 1979. Furthermore, the Economic Report also recommends that the Government consider undertaking a comprehensive reform of the financial system. Such a reform would play an important complementary role in improving the performance of the industrial sector. The Government has informed the Bank in a series of discussions over the past few months that it is in general agreement with these policy recommendations and is committed to undertaking a major reform of the financial system.

2.41 The inefficiencies identified in the Bank's review of the industrial and financial sectors transcend individual financial institutions. While past DFC lending has been efficient and has helped reach lending objectives, the changed circumstances facing the economy and the expanding demands placed on financial intermediaries suggest that the Bank's involvement in financial issues needs to be broadened from the narrow

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<sup>/1</sup> "Current Developments and Policy Issues," dated May 20, 1980.



project focus of the past. The Bank has acquired detailed knowledge of the workings of the financial system and is in the process of developing, in collaboration with the Korean authorities, the blueprint of a scheme designed to make the system more responsive to the needs of a rapidly maturing industrial sector which operates in an increasingly competitive international environment.

2.42 Bank lending for industry should now be tailored to accommodate these broader sectoral objectives. While the format of industrial lending will retain the past DFC lending approach, these operations will be used as a springboard for reaching other important objectives beyond resource transfer and institution-building objectives. Taking advantage of the simultaneous need to replenish the long-term foreign exchange resources of KDB and KDFC, the Bank invited the Government to negotiate both loans at the same time as a vehicle for discussing further the financial sector policy recommendations. A common understanding was reached at negotiations regarding Korea's longer-term strategy for improving efficiency in the financial sector. As a first step, a package of specific policy measures and supplementary studies to be implemented by the Government and KDB over an appropriate time frame was agreed upon which would provide a linkage between financial sector issues and the proposed KDB and KDFC operations. The proposed projects would support the first stage of a comprehensive reform of the financial sector. At negotiations, agreement was reached with the Government on a "Statement of Korea's Financial Sector Policy Improvements" expressing the broad objectives of the financial sector reform and outlining a number of policy measures to be implemented in an agreed time frame. Other financial sector issues, requiring further study will be discussed with the Korean Government in the context of forthcoming Structural Adjustment Loans and future financial sector loans.

### 3. THE KOREA DEVELOPMENT BANK

#### KDB's Role in the Industrial and Financial Sectors

3.01 KDB was established in 1954 as a wholly government-owned institution to implement, on behalf of the Government, post-war rehabilitation of industry and to finance economic development. Since then, KDB has been used by the Government as one of its primary agencies for the execution of the Five-Year Plan's industrial policies. At present, all major government-directed programs for industrial financing are, at least in part, being channelled through KDB with the exception of the short-term export credit program. In addition to supporting industry, KDB is called upon to finance major projects in the transportation and power sectors.<sup>/1</sup> Only large-scale <sup>/2</sup> enterprises are eligible for financial assistance from KDB.<sup>/3</sup> KDB's financing, however, is not confined to public sector projects; loans to the private sector have increased as a share of KDB's loan portfolio from 38% at end-1975 to 52% by end-1979. However, a major proportion of KDB's lending to the private sector is absorbed by large industrial conglomerates involved in priority activities with the full backing of the Government. At end-1979, KDB's portfolio comprised 561 clients; the 50 largest accounted for 86% of KDB's total portfolio.

3.02 KDB is the single largest financial institution in Korea and the largest source of term financing for industry. At end-1979, its total assets <sup>/4</sup> reached W 6,624 billion and accounted for 14.2% of the total assets of the financial sector. As of December 31, 1979, KDB's loan portfolio amounted to W 2,138 billion with the manufacturing accounting for 49.8%. KDB alone contributed about 18% of the increase in total outstanding loans (both short and long term) to the manufacturing sector in 1979 compared to 55% for

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<sup>/1</sup> At end-1979, the non-manufacturing sector accounted for 50.2% of KDB's outstanding portfolio and the crucially important power sector for about 25%.

<sup>/2</sup> i.e. enterprises employing more than 300 persons and with total assets exceeding W 500 million.

<sup>/3</sup> Smaller enterprises (employing less than 300 persons or with assets lower than W 500 million) receive financial assistance from the Small and Medium Industry Bank (SMIB) or from the Citizens National Bank (CNB) when employment is under 100 persons. Both institutions are government-owned.

<sup>/4</sup> Including guarantees outstanding for W 3,722 billion.

the group of 15 commercial banks. KDB's lending is geared primarily towards long term financing of equipment purchases; working capital loans accounted for only 17.5 % of KDB's aggregate commitments over 1976-79. Over the same period, KDB contributed 31.7% of the increment in outstanding term loans to the manufacturing sector compared to 27.4% for commercial banks. In 1979, KDB's loan commitments totalled W 955.7 billion (\$1.97 billion) of which 21% was in foreign currency. Loan guarantees extended during the same year reached W 1,142 billion with 94% in foreign exchange. KDB is less active in equity investment and subscription to debentures;<sup>/1</sup> its outstanding investment portfolio, however, amounted to W 332 billion as of December 31, 1979.

### Institutional Aspects

3.03 A detailed analysis of KDB's legal set-up, organization, operations and financial performance is provided in Annex B. This description shows that KDB has gradually built up its institutional capability to a very satisfactory level and that its financial structure and performance are sound. The salient institutional features of KDB are summarized below.

3.04 Scope of Operations. KDB is authorized to provide its clients with a comprehensive range of financial services including (a) domestic and foreign currency lending for equipment purchases; (b) working capital finance; (c) equity participation; (d) purchase of debentures; (e) issuance of loan guarantees; and (f) foreign exchange transactions. However, KDB's activities are focused primarily on equipment financing and issuance of guarantees. In these two areas, KDB has become the most active financial institution in Korea.

3.05 Branch Network. KDB's geographic reach outside the Seoul area is ensured through its ten branch offices. KDB has a branch office in the major cities of each of the eight mainland provinces and two other branches in the industrial areas of Ulsan and Changwon. About 15% of KDB's total professional staff of 584 was assigned to the branch offices at end-1979. Including nonprofessional staff, KDB employed a total of 1,960 persons at end-1979.

3.06 Appraisal and Supervision. The institution building impact of Bank lending to KDB over the past five years can best be gauged by the quality of KDB's project appraisal and supervision work as well as the soundness of its procurement and disbursement procedures. KDB's appraisal standards and procedures are quite satisfactory for projects funded from its own resources or from foreign official sources of funds including IBRD. The appraisal of projects funded with government resources tends to be less refined. Increasing emphasis has been placed by KDB in recent years on economic analysis and particularly on the employment impact of the projects it finances. Economic Rates of Return (ERR) are now calculated by KDB for projects funded from

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<sup>/1</sup> In 1979, total investments reached W 58.7 billion; equity participations accounted for 46%.

official borrowings and requiring financing of more than \$750,000 and for all other projects whose cost exceeds W 2 billion. KDB is well equipped to carry out extensive economic and industrial sector research having a Research Department comprising close to 70 professionals. KDB's project supervision work is thorough and effective as reflected in the good quality of its portfolio.

3.07 KDB's procurement and disbursement practices are sound. ADB and the Bank have helped KDB strengthen its procedures. Procurement methods comprise international competitive bidding, limited competitive bidding and proprietary contracts when justified.<sup>/1</sup> Procedures are generally designed to ensure a reasonable degree of competition and the appropriate use of funds. Further details regarding KDB's procurement procedures may be found in Annex B, para. 2.09.

#### Financial Sector Development

3.08 The preceding paragraphs provide an analysis of KDB's role in the industrial and financial sectors through its resource transfer function and provide an insight into its institutional strengths and quality. A third measure of KDB's importance as a development institution is the impact it has achieved in developing and deepening the structure of the Korean financial system by sponsoring the establishment of several specialized financial institutions.

3.09 A leasing company, wholly owned by KDB was established in 1973 to lease industrial machinery to firms, particularly small-sized, which cannot afford outright purchases for lack of collateral. In 1977, KDB participated jointly with foreign financial institutions in the share capital of a new Korean merchant bank. A second merchant bank was established in 1979 with minority holdings by KDB. Finally, KDB has established two subsidiary investment banks outside Korea, one in New York (1977) and the other in Hong Kong (1979). The impetus thus given by the KDB to the diversification of the Korean financial system through the establishment of specialized nonbank financial institutions has widened the range of financial services available in Korea. The increased overseas representation of Korean financial institutions should also facilitate the resource mobilization efforts of Korean financial and industrial enterprises in foreign capital markets.

#### Resource Allocation

3.10 The following paragraphs aim at evaluating KDB's efficiency as a financial intermediary in terms of (a) its performance as an allocator of funds to productive projects in Korea, and (b) its ability to mobilize

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<sup>/1</sup> ICB was applied for 56% of all procurement contracts under the third Bank loan (1570-KO) in 1979; limited competitive bidding accounted for 17% of all procurement contracts and proprietary contracts for 27%.

resources, domestic and foreign, commensurate with the requirements of industry in Korea.

3.11 As indicated in para 3.01, KDB functions as the bulwark of the Government's system of directed and subsidized credits.<sup>/1</sup> KDB's allocation of funds, by virtue of its 100% government ownership, is largely subject to government direction not only with respect to sectoral lending targets but also with respect to allocation by term, by currency and, at times, by individual firms. Resources raised by KDB from foreign official sources of funds (IBRD, ADB, et al) are also allocated to priority sectors but KDB enjoys adequate autonomy in its allocational decisions at the project level.

3.12 KDB's performance in directing resources to government-defined priority areas is impressive: about 50% of its outstanding loan portfolio at end-1979 was in manufacturing; power and transportation accounted respectively for 25% and 17%. Lending patterns within manufacturing follow government priorities closely: heavy and chemical industries accounted for 77% of KDB's outstanding loans to manufacturing in 1979.

3.13 Loan guarantee operations are also subject to government directions; as of December 31, 1979 about 76% of KDB's outstanding guarantee portfolio was with government-owned entities or companies designated by the Government.<sup>/2</sup>

3.14 Directed Lending. KDB administers three types of directed lending which jointly represent approximately 75% of its loan portfolio. The degree of government directives imposed on KDB's fund allocation varies in each case. The source of funding also varies in each case although some projects can be financed with a mix of the three types of resources. First, KDB is used by the Government as a channel of budgetary allocations to specific public sector entities in industry and infrastructure. Typical examples are the Korea Electric Co. (KECO) and the Pohang Iron and Steel Company (POSCO) which, taken together, accounted for as much as 39% of KDB's total loan and guarantee portfolio at end-1979. Funding of these operations is about half from budgetary appropriations and half from National Investment Fund (NIF)<sup>/3</sup> resources. In the administration of budgetary resources, KDB acts merely as a conduit of funds; individual allocations by firm are predetermined by the Government and therefore not subject to independent review by KDB.

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<sup>/1</sup> For an analysis of the system of directed and subsidized credits see paras. 2.19 through 2.22 above.

<sup>/2</sup> Guarantees issued by KDB to government-owned and designated enterprises are covered by a blanket counterguarantee (GRA) of the Government.

<sup>/3</sup> The NIF is analyzed in detail in Annex C and a summary description is given in the following paragraph.

3.15 The second type of directed/subsidized lending administered by KDB (and the DMBs) consists of several special government funding programs for financing industry. The NIF is the largest of these special funds /1 (para. 2.22). The NIF is managed by BOK and MOF. BOK is primarily responsible for funding the program while MOF directs allocational decisions. Specifically, MOF determines allocations at the broad sectoral level among power, heavy and chemical industry, food and small-scale industries. Allocation at the firm level is decided by the NIF Council which comprises representatives of EPB, MCI, BOK and KDB. About 82% of the 1980 NIF allocations were for preselected firms. The discretionary powers of handling banks in allocational decisions could be exercised fully on the 18% balance. In general, for NIF and other special funding programs, KDB's input in project formulation and appraisal comes late in the decision-making process, at times too late to have a meaningful impact on investment decisions. The somewhat negative implications of this situation should, however, be tempered in the light of the thorough scrutiny to which government agencies such as EPB /2 subject investment proposals for large-scale priority projects. The need for a rationalization of the operations of the NIF program was discussed at negotiations. It was agreed that KDB and the Government would jointly undertake a study to evaluate the NIF program. Further details relating to this agreement may be found in paras. 4.08-4.09.

3.16 A third type of directives is imposed by the Government on KDB's allocation of funds from resources raised independently from the Government's budgetary and special fund appropriations. These resources consist of deposits, proceeds of KDB bonds and foreign currency borrowings. KDB is expected to allocate these resources in accordance with government priorities defined in the 1953 KDB Act and its Enforcement Decree, i.e., power, coal mining, shipbuilding, iron and steel, semiconductors, marine and air transportation. Project-by-project allocation is determined by KDB within global sectoral lending targets fixed annually in KDB's Operational Program with the agreement of MOF. In practice, only foreign loans funded from official borrowings are immune from strict government directives but the priority manufacturing sector does absorb a large proportion of the funds. Government-directed lending accounts for about 60% of the resources raised independently by KDB./3

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/1 The NIF was established in 1973 in replacement of the Industrial Rationalization Fund (IRF) initiated in 1972; other programs include the Special Long-term Fund of 1972 and the Tourism Development Fund (TDF) which is onlent by KDB to the commercial banks.

/2 EPB's Project Evaluation Bureau employs 40 persons specialized by sector.

/3 Excluding foreign official funds; loans funded with resources raised independently by KDB accounted for approximately 37% of the end-1979 loan portfolio.

3.17 The following table shows a breakdown of KDB's outstanding loan portfolio in 1977-79 by source of funds. Government-funded loans <sup>/1</sup> accounted for approximately 55% of KDB's loan portfolio during that period. The supplementary directives imposed by the Government on the allocation of resources raised independently by KDB brought aggregate directed policy loans to about 75% of KDB's end-1979 loan portfolio.

KDB's LOAN PORTFOLIO BY SOURCE, 1977-79  
(W billion)

December 31,	1977		1978		1979	
	Amount	%	Amount	%	Amount	%
<u>Government Funding</u>						
Special funds	367.5	36.5	609.4	42.2	892.2	41.7
Budgetary resources	166.7	16.5	221.0	15.3	270.4	12.6
Subtotal	<u>534.2</u>	<u>53.0</u>	<u>830.4</u>	<u>57.5</u>	<u>1,162.6</u>	<u>54.3</u>
<u>KDB-raised Resources</u>						
Domestic currency	197.3	19.6	241.9	16.8	330.0	15.4
Foreign commercial borrowings	172.1	17.1	225.0	15.6	466.3	21.8
Foreign official borrowings	104.2	10.3	146.2	10.1	179.1	8.4
Subtotal	<u>473.6</u>	<u>47.0</u>	<u>613.1</u>	<u>42.5</u>	<u>975.4</u>	<u>45.7</u>
<u>Total</u>	<u>1,007.8</u>	<u>100.0</u>	<u>1,443.5</u>	<u>100.0</u>	<u>2,138.0</u>	<u>100.0</u>

3.18 Quality of Portfolio. Despite government controls and intervention in lending decisions, KDB has retained enough autonomy in its allocative decisions to select creditworthy borrowers and maintain a satisfactory quality of portfolio. At end-1979, 89.8% of KDB's total loan portfolio was outstanding with companies operating profitably; <sup>/2</sup> companies in difficulty and operating at a loss accounted for 8.7% and companies in liquidation for 1.5%. At the same date, the principal of loans affected by arrears over three months amounted to W 149 billion or 7% of the total outstanding loan portfolio. In 1979, KDB rescheduled a number of overdue loans with an aggregate outstanding balance of W 160 billion or 7.5% of the end-of-year portfolio. In total, 14.5% of KDB's total portfolio was either rescheduled or in arrears in 1979. Comparative figures for 1978 were 2.9% for principal affected by arrears over three months and 3.3% affected by reschedulings, or a total portfolio affected of 6.2%.

<sup>/1</sup> i.e., with Government special funds and budgetary resources.

<sup>/2</sup> In 1978 the ratio was 93%.

3.19 While the year 1979 was marked by a deterioration of the financial health of some of its borrowers, KDB's loan portfolio remained very sound. Actual arrears of interest and principal (in excess of 3 months) remained at a very low level of 0.5% of total portfolio at end-1979.<sup>/1</sup> The higher level of principal affected (7%) reflected the high exposure of KDB in the companies it finances either because individual loan size is large or because several loans are outstanding with a single borrower. The still satisfactory quality of KDB's portfolio indicates that KDB does operate as an efficient allocator of funds. The deterioration in the financial performance of some KDB borrowers does not appear to be linked to the system of government-directed/subsidized lending but is rather a reflection of the sluggish economic performance of industry in 1979.

3.20 The system of directed/subsidized lending, however, does have a negative impact on KDB's exposure in individual firms. Although it is KDB's stated policy not to provide financial assistance in excess of 65% of the total assets of a borrower, at end-1979, the limit had been exceeded for 15 large government-owned or government-supported firms. As much as 57% of KDB's aggregate loan, investment and guarantee portfolio was outstanding with these 15 firms. A system of guarantees and counter-guarantees granted to KDB by the Government <sup>/2</sup> effectively protects KDB from the financial risks caused by such overexposure. Despite this protection given to KDB, government pressures to increase financial assistance to some borrowers are clearly conducive to high debt/equity ratios in industry and help maintain an unsound financial structure. In order to improve the financial structure of its subborrowers and its own exposure in individual firms, an understanding was reached during negotiations that only enterprises whose total debt/equity ratio (including the proposed subloan) was not greater than 5:1 would be eligible for financing under the proposed Bank loan.

3.21 As indicated above, subsidized lending, because of the artificially cheap cost of credit, may also be conducive to excessive loan demand, inadequate pricing of capital and suboptimal choices of technologies. At end-1979, 91% of KDB's outstanding domestic currency loans carried subsidized lending rates. KDB being the main agent of the system of directed/subsidized lending has not always been granted by the Government enough autonomy in its allocational decisions to mitigate through careful appraisal work the negative effects of inadequate pricing of capital for priority industries.

#### Resource Mobilization

3.22 The ability of a financial institution to mobilize adequate amounts of resources is another indicator of its efficiency as a financial intermediary. KDB's performance at mobilizing financial resources through direct borrowings and indirectly through issuance of loan guarantees, has been

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<sup>/1</sup> Compared to 0.3% at end-1978.

<sup>/2</sup> Guarantees are granted under the "Guarantee Release Arrangement" dated March 31, 1975 and the Supplemental Letter dated December 23, 1976.



very impressive, particularly in the past four years. The increase in KDB's outstanding borrowings and guarantees over 1976-79 amounted to W 3,945 billion or approximately 50.4% of the cumulative current price fixed investment in manufacturing and power. Out of the aggregate W 3,945 billion, net increase in borrowings accounted for 43% and guarantees for 57%.

3.23 KDB's outstanding liabilities have grown at an average of 48% p.a. over 1977-79 and reached the equivalent of \$4.64 billion by end-1979. The following table shows the composition of KDB's borrowings and loan portfolio over the period 1975-79.

TOTAL OUTSTANDING BORROWINGS OF KDB (1975-79)  
(Won billion)

December 31,	1975		1976		1977		1978		1979	
	Amt.	%	Amt.	%	Amt.	%	Amt.	%	Amt.	%
<u>Domestic</u>										
<u>Currency</u>										
Deposits & debentures	94.1	17.2	81.3	11.4	148.0	15.1	200.6	13.8	253.8	11.3
Budgetary resources	149.1	27.2	168.6	23.6	202.2	20.7	262.5	18.1	311.9	13.9
Special funds	168.3	30.7	258.6	36.2	354.1	36.2	602.6	41.4	880.8	39.1
Subtotal	<u>411.5</u>	<u>75.1</u>	<u>508.5</u>	<u>71.2</u>	<u>704.3</u>	<u>72.0</u>	<u>1,065.7</u>	<u>73.3</u>	<u>1,446.5</u>	<u>64.3</u>
<u>Foreign</u>										
<u>Currency</u>										
Deposits	35.2	6.4	21.0	2.9	11.2	1.1	-	-	0.5	-
Official sources	36.1	6.6	66.4	9.3	100.4	10.3	146.0	10.0	178.3	7.9
Commercial sources	64.8	11.9	118.7	16.6	162.6	16.6	241.2	16.7	624.9	27.8
Subtotal	<u>136.1</u>	<u>24.9</u>	<u>206.1</u>	<u>28.8</u>	<u>274.2</u>	<u>28.0</u>	<u>387.2</u>	<u>26.7</u>	<u>803.7</u>	<u>35.7</u>
<u>Total</u>										
<u>Out-</u>										
<u>stand-</u>										
<u>ing</u>	<u>547.6</u>	<u>100.0</u>	<u>714.6</u>	<u>100.0</u>	<u>978.5</u>	<u>100.0</u>	<u>1,452.9</u>	<u>100.0</u>	<u>2,250.2</u>	<u>100.0</u>

TOTAL OUTSTANDING LOAN PORTFOLIO OF KDB (1975-79)  
(Won billion)

Dec. 31,	1975		1976		1977		1978		1979	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Domestic currency loans	528.8	91.5	665.3	89.9	902.6	89.6	1,239.3	85.9	1,814.6	84.9
Foreign currency loans	49.0	8.5	74.6	10.1	105.3	10.4	204.2	14.1	323.5	15.1
<u>Total</u>	<u>577.8</u>	<u>100.0</u>	<u>739.9</u>	<u>100.0</u>	<u>1,007.9</u>	<u>100.0</u>	<u>1,443.5</u>	<u>100.0</u>	<u>2,138.1</u>	<u>100.0</u>

3.24 The share of domestic currency resources in KDB's total borrowings has declined from 75.1% in 1975 to 64.3% in 1979. Foreign currency commercial borrowings have grown very rapidly in absolute and relative terms; this rapid growth accounts for the increasing share of foreign currency resources in KDB's total resources. The above tables also show that the demand for domestic currency funding, as reflected in the size of the domestic currency loan portfolio, substantially exceeded the level of domestic resources available to KDB through its own mobilization efforts and through government appropriations. In order to supplement its otherwise insufficient domestic currency resources, KDB has been mobilizing foreign currency resources substantially exceeding its foreign currency lending and has converted part of the commercial borrowings into Won resources to finance the higher demand for domestic currency funds. Foreign currency borrowings from official sources have not been converted into domestic currency resources. Their long maturity relative to foreign commercial funds makes foreign official borrowings particularly attractive to an institution like KDB whose function is to finance a number of large priority projects having a long gestation period. Because of the floating interest rate attached to foreign commercial borrowings and the foreign exchange risks associated with conversions into Won, KDB onlends these funds at an interest rate which is revised quarterly and takes account of past foreign exchange fluctuations./1

/1 For the second quarter of 1980, the lending rate was fixed at 13.6% for priority industries and 17.1% for nonpriority projects.

The magnitude of conversions into domestic currency is reflected in the 15.1% share of foreign loans outstanding in KDB's total portfolio compared to the 36% share of foreign borrowings in total borrowings.

3.25 Domestic Currency Resource Mobilization. Budgetary appropriations and special government funds provide the bulk of KDB's domestic currency resources. Their combined share of KDB's total domestic resources has increased from 77.1% in 1975 to 82.5% in 1979 because of the slower growth of other sources of domestic resources, i.e., deposits and domestic currency debentures. Budgetary funding and special fund resources are allocated to KDB by the Government when finalizing the annual Operational Program. KDB's independent mobilization efforts consist of deposit taking and issuance of debentures. By law, KDB is authorized to take deposits from its corporate borrowers only. Unlike DMBs, which take deposits from the general public, KDB's deposits therefore account for a minor part of total domestic currency resources.

3.26 Issuance of domestic currency Industrial Finance Debentures (IFDs) is viewed by KDB both as a means of raising additional resources and as contributing to the lengthening of maturities in the securities market. KDB issues discount debentures with maturities of one to three years and coupon debentures with a five-year maturity. Over the past few years, KDB has issued increasing amounts of debentures; the face value of new issues has risen from W 50 billion in 1977 to twice that amount in 1979. Redemption of previous issues reached an average of 46% of new issues over 1977-79; net outstanding debentures have consequently risen from W 79.5 billion at end-1977 to W 143.2 billion at end-1979. These amounts are far from negligible but represent no more than 6-8% of KDB's total borrowings during the period 1977-79.

3.27 KDB's limited reliance on debenture issues to cover its domestic resource requirements is due to the high cost of this type of funding. Since January 1980, nominal yields on KDB debentures range from 17.8% to 24% and effective yields reach 27.88% to 29.13%./1 By comparison, KDB's highest lending rate is 26.5% p.a. for nonpriority borrowers. Onlending the proceeds of debentures therefore implies a negative interest spread of about 2 percentage points. In practice, KDB has been onlending part of these resources to priority borrowers at concessional interest rates, thus increasing the negative spreads.

3.28 The yield on KDB bonds is subject to MOF approval and appears adequate given current interest rates on time and savings deposits./2 Since Korean authorities rightly feel that KDB should continue and increase its

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/1 Because interest is payable semiannually at front.

/2 Twenty-five to 26% p.a.

issuance of domestic currency debentures, at negotiations it was agreed that the Government would take the action necessary on its part to enable KDB to onlend the proceeds of its domestic debentures with a positive interest spread. A possible means of achieving a positive spread would be to allow KDB to increase its effective lending rate to about 30% p.a. by charging interest in advance. This practice is widespread among other Korean financial institutions and would be in line with the method of interest payments on IFDs./1

3.29 Foreign Currency Resource Mobilization. KDB has been extremely successful in mobilizing increasing amounts of foreign currency resources over the past few years, both from official and commercial sources. The following table summarizes KDB's borrowing performance on a commitment basis through 1979.

FOREIGN CURRENCY BORROWINGS BY KDB (1966-79)  
(in US\$ million)

	1966-73	1974	1975	1976	1977	1978	1979	Total
Official sources	74.3	30.0	117.5	102.8	-	160.0	-	484.6
Foreign commercial banks	25.0	80.0	-	98.6	-	250.0	711.1	1,164.7
Foreign currency debentures	-	19.9	-	69.2	82.9	41.7	43.9	257.6
<u>Total</u>	<u>99.3</u>	<u>129.9</u>	<u>117.5</u>	<u>270.6</u>	<u>82.9</u>	<u>451.7</u>	<u>755.0</u>	<u>1,906.9</u>

3.30 KDB's first \$25 million commercial borrowing was contracted in 1970. Since then, KDB has been mobilizing increasing amounts of foreign commercial resources and has issued foreign currency debentures (eurobonds). KDB's latest commercial borrowing of \$600 million in 1979 was obtained on very favorable terms./2 Another "jumbo" loan of \$600-700 million is

/1 A nominal interest rate of 25.5% p.a. with quarterly interest payments at front would be equivalent to an effective rate of 30.15% p.a.

/2 LIBOR + 0.625 in the first five years and LIBOR + 0.75 in the following five years.

contemplated in 1980. KDB's reliance on official sources of funds which reached 75% of total foreign borrowings over the period 1966-73 has rapidly declined to 22.7% over 1974-79. A further reduction is contemplated in coming years.

3.31 Official sources of funds (ADB, IBRD and KfW) provided a total of \$380.3 million in 1975-79; this covered about 44% of KDB's total foreign currency commitments over that period. Aggregate commercial borrowings of \$1,297.4 million (in 1975-79) covered the resource gap and provided excess funding of about \$800 million. As indicated in para. 3.30, excess commercial borrowings have been converted into domestic currency to support KDB's Won lending operations.

3.32 KDB's practice of utilizing part of its foreign commercial borrowings to finance domestic currency operations results from a conscious policy decision endorsed by the Government. The reasons for this practice are twofold: (a) opportunity cost of foreign capital versus domestic capital; and (b) balance-of-payments support.

3.33 The mix of floating rate dollar borrowings and fixed rate Yen borrowings brought the average cost of KDB's outstanding foreign commercial funds to 14.46% in the second quarter of 1980. Alternative sources of domestic currency resources consist primarily of domestic currency IFDs which have a cost to KDB of 28-29% (para. 3.27). Given comparative costs, it seems that, at present, KDB's conversion of commercial borrowings into domestic currency is based on good financial management. The conversion by KDB of part of its foreign commercial borrowings into won through deposits at BOK has also provided effective support to Korea's balance of payments. In the longer run, however, increased domestic savings are desirable for the country and KDB should be encouraged by the Government to mobilize more domestic resources by issuance of domestic IFDs. It would therefore make good economic sense to improve the attractiveness to KDB of IFD funding.

3.34 Despite the increased exposure of the Korean commercial banks in Eurocurrency markets, the bulk of the commercial banks foreign exchange resources is supplied by the central bank. Initially, KDB was expected to onlend part of its \$600 million commercial borrowings of 1979 to other Korean financial institutions with little or no credit standing in the Eurodollar markets. This apex mechanism did not materialize because of pressures on Korea's balance of payments. Part of the funds /1 was credited to the BOK to finance, in part, the current account deficit in the balance of

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/1 \$200 million has been deposited with BOK. The Monetary Stabilization Bonds issued by BOK against this deposit can be repurchased by KDB at a future date to finance its lending operations.

payments. In effect, KDB has raised commercial foreign exchange resources not only for its own purposes, but also for meeting the general needs of the economy. A similar mandate has been given by the Government to the Korea Exchange Bank in 1979 and 1980. A portion of the \$600 million commercial borrowing which KDB plans to raise in 1980 may also be earmarked to cover part of the projected \$6.0 billion deficit in the balance of payments. This new mandate imposed on KDB by the Government gives it two separate functions: (a) the provision of development finance for the industrial sector, and (b) borrowing agent for the Korean Government in international capital markets. The apex concept might be revived in the future since the Government feels that the system of permitting only a limited number of institutions with good credit standing to borrow abroad avoids an unnecessary competition for funds which could otherwise lead to less advantageous terms.

### Conclusion

3.35 The preceding description and analysis of KDB's role and institutional efficiency in the industrial and financial sectors shows that KDB qualifies as a well managed and operated financial institution. A more detailed review of KDB's operations and performance is given in Annex B. Shortcomings have been identified which relate primarily to: (a) insufficient domestic currency resource mobilization; (b) KDB's insufficient contribution to the efficient allocation of resources for operations funded by the Government; and (c) the negative impact of the system of directed/subsidized lending on the financial structure of the corporate sector.

3.36 These issues transcend the narrow institutional framework of KDB and raise more fundamental questions about the efficiency of Korea's financial system. These issues have been elaborated upon in Chapter 2. It is expected that the proposed loan would set the basis for a continuing exchange of views with the Government on broad financial sector issues and would provide an opportunity for specific measures to be adopted by the Government as a first step toward improved efficiency in the sector.

#### 4. THE PROPOSED BANK LOAN

##### A. Objectives of the Proposed Loan

4.01 The proposed \$100 million loan to KDB would have the the following four major objectives: (a) resource transfer to the industrial sector; (b) continued upgrading of the institutional capability of KDB to operate as an efficient financial intermediary; (c) improvement in the operations of the financial sector as a whole; and (d) improvement in the financial structure of the corporate sector.

##### Resource Transfer

4.02 Despite the satisfactory level of domestic savings in Korea, continued reliance on foreign savings to which the proposed loan would contribute is essential for pursuing the structural transformation of industry. To the extent that "DFC" type projects are quick disbursing, the proposed loan would also contribute substantially to reducing the heavy balance-of-payments deficits expected in the next few years.

4.03 The proposed \$100 million loan would be the fourth lending operation of the Bank to KDB. The proposed loan would cover a minor portion of about 10% of KDB's projected aggregate foreign currency loan commitments over the two-year period 1981-82.<sup>/1</sup> The relatively small contribution of the Bank loan to KDB's resource requirements is justified by KDB's increasing ability to mobilize foreign resources from commercial sources. KDB's reliance on foreign official borrowings has declined in the past few years and is expected to decline further. However, the average maturity of the subloans made by KDB is about 8 years at present and KDB therefore tends to limit its mobilization of commercial borrowings to lines of credit having an 8-10 year maturity. Under the proposed loan, the Bank would agree to fit the amortization of its funds around shorter-term market borrowings for subprojects co-funded with commercial and Bank resources. It is expected that this dovetailing of repayments would allow KDB not to limit its commercial borrowings to resources having a maturity of at least 8 years; the proposed feature would allow the use of shorter-term (4-5 years) commercial resources in the financing of long-term loans thereby increasing the availability of long-term resources in the economy. The increase in the flow of commercial funds would help reduce the share of official resources in KDB's total foreign borrowings.

4.04 Interest Spread on Commercial Borrowings. Until June 1980, the maximum interest spread which financial institutions could charge for handling official and commercial foreign resources was fixed by the Government at 2%

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<sup>/1</sup> Foreign currency loan commitments are projected at \$987 million over 1981-82.

and 0.5% respectively. This discrepancy effectively discriminated against increased mobilization of foreign commercial resources and did not take into account the magnitude of administrative expenses of financial intermediaries.<sup>/1</sup> During negotiations, Government representatives pointed out that as of June 1980, an interest spread of up to 2% on foreign commercial resources was authorized by the Government. It was agreed that this measure would become effective for KDB no later than March 1, 1981.

4.05 The higher interest spread on foreign commercial borrowings and the proposed adjustment of repayments to the Bank for cofunded subloans is expected to reduce substantially KDB's reliance on official sources of funds. A complete phasing out of Bank lending to KDB, however, does not seem feasible nor desirable in the near future. Although KDB has mobilized foreign commercial resources totalling \$1,300 million over the period 1975-79 compared to foreign currency loan commitments of only \$900 million, it had to rely on additional borrowings from official sources of about \$400 million. The reason for this apparent contradiction <sup>/2</sup> lies in the longer maturity of official borrowings.<sup>/3</sup> KDB is currently unable to mobilize other resources, domestic or foreign, with a maturity exceeding 10 years. An increasing number of projects in the priority areas of heavy industry however, have a long gestation period and therefore require a loan payback period exceeding 10 years.<sup>/4</sup> To a large extent, Bank resources have been earmarked for funding such projects.<sup>/5</sup> The restructuring of the Korean manufacturing sector toward

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<sup>/1</sup> Approximately 1% of average assets.

<sup>/2</sup> Aside from the need for KDB to fund part of its domestic currency lending operations from the proceeds of foreign commercial borrowings (para. 3.30).

<sup>/3</sup> Up to 15 years.

<sup>/4</sup> Over the period 1977-79, KDB's total commitments of loans with a maturity exceeding 10 years reached about \$529 million, or approximately 16% of total loan commitments during this 3-year period.

<sup>/5</sup> The weighted average maturity of subloans financed by KDB under Bank loan 1574-KO was 11.4 years compared to an overall average of 7.9 years.



heavy industry will be pursued in coming years thus necessitating the continued availability of long-term resources. Until such long maturity funding is available from commercial sources, some reliance on foreign official resources will be required.

#### Institution Building

4.06 Institution building is a major objective of DFC-type operations. In this instance, the Bank has already had, through previous loans, an effective impact on improving the administrative and institutional capacity of KDB. This impact, however, was primarily focused on financing operations involving the use of Bank resources. The proposed project would support increased efficiency of KDB in channeling Bank and other resources. Specifically the project would aim at strengthening KDB's role as the agent of the Government for industrial lending programs including the National Investment Fund. The concentration of NIF lending within the specialized banks and KDB which was agreed upon during negotiations and is further explained in paras. 4.08-4.09 would ultimately aim at more than a simple rationalization of lending mechanisms. KDB has agreed to establish within its present organization a special unit in charge of monitoring the impact of NIF lending. The objective would be to build up KDB's capability to assist the Government in evaluating the efficiency of its lending programs and to help formulate/adjust lending policies and financing patterns accordingly. It is also expected that, over time, KDB would be given increased latitude to apply the same selection criteria in fund allocation under government programs as it currently does for Bank-funded subprojects.

#### Financial Sector Objectives

4.07 The Government is fully aware of the shortcomings of the Korean financial system and has indicated its firm intention to move gradually toward restructuring the sector. The Government's long-term objective is to liberalize the operations of financial institutions, particularly commercial banks, in order to induce more competition and efficiency in the financial sector. Increased reliance will be placed on flexible tools of financial management as opposed to the present rigid system of directing fund allocations and tightly controlling financial institutions. The Government has specifically expressed its intention to: (a) keep real interest rates at a positive level; (b) to reduce the scope of concessional directed lending; and (c) to liberalize the operations of commercial banks. The proposed loan provided the Bank with an opportunity to agree with the Government on a set of specific policy measures which represents a first step toward achieving the longer-term objectives described above. The preceding review of the Korean system of long-term industrial financing (Chapter 2) and of the role played by KDB as the largest financial institution operating in that system (Chapter 3) suggests three areas of action: (a) rationalization of the system of government directed lending through a reorganization of its major component (for which KDB is the main agent), i.e., the National Investment Fund program; (b) enhanced mobilization of domestic currency resources by KDB; and (c) rationalization of foreign currency lending rates.

4.08 The National Investment Fund. The operations of NIF are described in Annex C. As KDB administers a major part (two thirds) of NIF lending, it was considered appropriate to discuss the rationalization of the NIF program with the Korean Government in the context of the fourth loan to KDB. The major deficiency of the program stems from its availability for a number of too broadly defined priority areas including heavy industries, export financing and the purchase of domestically manufactured machinery. Both the Bank and the Government recognize that it is necessary to better define and to restrict priority sectors eligible for NIF's subsidized resources. In light of this mutual understanding, it was agreed during negotiations that the Government would undertake an evaluation of the NIF program which would include detailed industrial sectoral and subsector studies designed to redefine priority areas for NIF lending. By narrowing the focus of NIF lending to clear priority industries identified through these sectoral studies, a reduction in NIF lending relative to total industrial lending would occur. This would reverse the trend of past years towards larger NIF operations which impose an increasing burden on government finances because of the interest subsidy on NIF loans.

4.09 As the extent of NIF lending is reduced, there would also be a need to restrict its administrative scope to institutions directly controlled by the Government, i.e. the specialized banks and KDB. The commercial banks which currently handle only 20% of NIF lending could be freed from this type of government-directed lending which would be in line with the Government's stated objective of liberalizing the operations of commercial banks. In this regard, the Government agreed at negotiations to gradually reduce, and eventually cease the provision of NIF resources to the commercial banks. A further understanding was reached during negotiations that given the enhanced role of KDB in NIF lending, KDB would establish a special unit to monitor the overall impact of NIF lending and to administer KDB's own lending activities under the program. This unit would also provide support to the Government's evaluation of the NIF program. Further discussion on the supplementary analytical work the Bank feels is necessary to support the rationalization of the NIF program over time is presented in Annex C. The terms of reference of the detailed study of the NIF program to be implemented jointly by the Government and KDB are to be furnished to the Bank by March 31, 1981, and the study is to be completed by December 31, 1981.

4.10 Mobilization of Domestic Currency Resources. KDB has been issuing considerable amounts of domestic currency debentures over the past years but has been compelled by government interest rate regulations to onlend the proceeds with a negative interest spread (para. 3.27). Increased issuance of domestic currency debentures has, therefore, been limited by the sizeable losses incurred by KDB in onlending IFD proceeds. Debentures are practically the only source of domestic currency resources for KDB, aside from the Government's special funds and budgetary resources; net issuances of IFDs, however, provided no more than 22% of the domestic currency funding needs of KDB over 1977-79.<sup>/1</sup> Insufficient domestic currency resources have compelled

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<sup>/1</sup> Net of lending operations funded by special funds and budgetary allocations.

KDB to convert part of its foreign commercial borrowings into Won in order to cover its shortage of domestic currency resources (para. 3.33). This recourse is questionable and a more satisfactory long-term solution was discussed and agreed upon with the Government during negotiations. The Government will now take the actions necessary to enable KDB to onlend the proceeds of its domestic debentures with a positive interest spread.

4.11 Rationalization of Foreign Currency Lending Rates. As indicated in para. 2.34, the current practice of imposing a uniform interest spread of 2% on the cost of foreign official borrowings results in unjustified distortions of final lending rates. The suggestion made during negotiations that each institution apply a spread of 2% to the weighted average cost of its borrowings was agreed upon.

#### Corporate Financial Structure

4.12 The high indebtedness of Korean enterprises results in part from excessive short-term borrowings and insufficient capitalization. KDB is in a position to make its financial assistance conditional upon higher equity contributions by project sponsors and to assist in strengthening the financial structure of its borrowers. An objective of the proposed loan would be to limit access to Bank and other resources to enterprises which are committed to improving their financial structure and qualify under a specific total debt/equity ratio. As discussed in para. 3.20, eligibility for financing under the proposed Bank loan would be limited to enterprises whose total debt/equity ratio does not exceed 5:1.

#### B. Benefits

4.13 The principal justification for the proposed loan is the expected beneficial impact of the selective policy measures described above on the operations of the financial sector as a whole. The loan would also provide a vehicle for initiating discussions between the Bank and the Government on a comprehensive reform of the financial sector. The policy dialogue would be continued during supervision of the proposed loan and formulation of subsequent industrial sector loans. The package of policy measures linked to the proposed loan would constitute the first phase of a comprehensive reform of the financial sector.

4.14 The proposed loan would be disbursed through KDB to qualifying subprojects in the industrial sector. Experience with previous lending through KDB shows that the projects financed with Bank resources have yielded substantial economic benefits. Sample ERR calculations show a range

of 13% to 46%. The subprojects to be financed under the proposed loan are expected to yield similar economic benefits. The proposed loan does not entail any unusual risk.

### C. Main Features of the Loan

4.15 Purpose. As with previous Bank loans to KDB, the proposed loan would be used to finance (a) 100% of the foreign exchange cost of directly imported goods and services and (b) 60% of the cost in domestic currency (representing the estimated foreign exchange component) of locally manufactured or procured machinery and equipment. Procurement would be in accordance with KDB's standard procedures which are satisfactory. The procurement procedures of KDB are designed to ensure a sufficient degree of competition and reasonable costs. The Bank is satisfied with the performance of KDB in dealing with procurement matters under previous Bank loans.

4.16 Amortization Schedule. As is usual with Bank loans to DFCs, the proposed loan would have an adjustable composite amortization schedule reflecting the aggregate amortization schedules of the subloans made by KDB.

4.17 The proposed loan is expected to be fully repaid within 15 years including a grace period of three years. Individual subloans (with the exception of cofunded subloans) would have a maximum maturity of 13 years including a grace period of three years. As indicated in para. 4.03, the Bank would encourage the use of its funds as a catalyst for increased mobilization of medium-term foreign commercial borrowings. It is therefore expected that some of the subloans would be co-funded with Bank resources and with shorter-term (4 to 5 years) commercial borrowings. In the case of co-funded subloans, the Bank would agree to fit the amortization of its funding around the (earlier) maturities of commercial funds. Normal Bank practice is to require approximately equal installments of principal for each subloan.<sup>/1</sup> For co-funded subloans earlier repayments by the subborrower may be assigned in full to the amortization of commercial funds and repayments to the Bank may start thereafter, thus implying a grace period of up to 5 years on Bank funds. A disbursement schedule for the proposed loan is provided in Annex B, Table 26.

4.18 Free Limit. Under the third Bank loan to KDB, the free limit for subloans not requiring prior Bank approval was set at \$2.5 million. The standards of operations of KDB would justify a complete waiver of the free

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<sup>/1</sup> Or equal installments of principal and interest.

limit. KDB, however, finds some merit to the exchange of views taking place through Bank reviews of subloans above the free limit. It is recommended that the free limit be increased to \$5 million. This limit is expected to result in approximately 40% of the proposed loan being allocated to subprojects requiring detailed review by the Bank prior to approval.

4.19 Subloan Ceiling. To ensure that the proceeds of the previous Bank loan to KDB were spread over a relatively large number of projects, a ceiling of \$7.5 million was imposed on individual subloans. A subloan ceiling of \$10 million is recommended under the proposed loan in view of the size of some of the heavy industry projects financed by KDB.

4.20 Debt/Equity Limit. Previous Bank loan agreements impose, since July 1979, a limitation of 10 times on the ratio of KDB's debt <sup>/1</sup> relative to equity. This limit is considered adequate and no change is therefore proposed.

4.21 Relending Rate. The relending rate will be based on the weighted average cost of foreign currency resources available for future lending, including the proposed loan. A 2% interest spread will be added to that average cost in determining the final lending rate to subborrowers. The Bank's practice to disburse a mix of US dollars and other currencies brought the effective cost in Won terms of Bank funds for the subborrowers (who bear the foreign exchange risk) to 17.4-26.5% p.a. for previous Bank loans to KDFC (para. 2.33). The effective cost to the subborrowers of Bank funds channelled through KDB under previous loans was in the same range. Assuming that past trends in foreign exchange fluctuations remain unchanged, and the effective lending rate in Won terms also remains unchanged as a consequence, the effective cost of Bank funds would be in line with that of foreign commercial resources and with the domestic currency lending rate. The effective lending rate would be positive in real terms and the proposed relending rate formula therefore appears adequate.

#### D. Agreements and Understandings Reached at Negotiations

4.22 During loan negotiations, the following agreements were reached with the Korean Government:

- (a) the Government would formulate a "Statement of Korea's Financial Sector Policy Improvements." The statement would express the broad objectives of the financial sector reform and specify a number of policy measures to be implemented over time (para. 2.43);

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<sup>/1</sup> Debt being defined as including long-term debt (with a maturity exceeding one year) and outstanding guarantees net of the portion for which the Government has issued a counter guarantee.

- (b) a specific time frame was discussed and agreed upon for completion of the financial policy measures and studies listed in the "Statement of Korea's Financial Sector Policy Improvements";
- (c) the package of policy measures linked to the proposed loan comprises (i) a reduction in the scope of priority activities qualifying for financing under NIF (para. 4.08); (ii) a restriction in the administrative scope of NIF lending to the specialized banks and KDB (para. 4.09); (iii) authorization for KDB to onlend the proceeds of its domestic currency debentures with a positive interest spread (para. 4.10); (iv) harmonization of lending rates for foreign currency funds raised from official resources (4.11); (v) a higher interest spread of up to 2% for onlending foreign commercial borrowings (4.04); and
- (d) a detailed study of the NIF program would be undertaken jointly by KDB and the Government and completed by December 31, 1981 (para. 4.09).

4.23 In addition, the following agreements and/or understandings were reached with KDB.

- (a) the final onlending rate for subborrowers is to be based on the formula agreed upon with the Government (para. 4.22(c)(iv) above);
- (b) KDB will establish within its present organizational setup a specialized unit in charge of monitoring the performance of NIF borrowers at a subsectoral and branch of industry level (para. 4.09);
- (c) Bank funds will be allocated to enterprises which are committed to improving their financial structure and qualify under a specific debt/equity ratio (para. 4.12);
- (d) the amortization schedule of subloans co-funded with commercial foreign borrowings will be adjusted (para. 4.17);
- (e) the free limit on subloans will be raised to \$5 million (para. 4.18);
- (f) a ceiling of \$10 million would be applied to individual subloans (para. 4.19); and
- (g) a long-term debt/equity ratio of 10:1 will be maintained by KDB (para. 4.20).

4.24 Recommendation. A Bank loan of \$100 million for a term of 15 years including a grace period of 3 years is recommended to be made to the Korea Development Bank.

KOREA

THE KOREA DEVELOPMENT BANK

ANNEX A: THE KOREAN FINANCIAL SECTOR

KOREA

ANNEX A: THE FINANCIAL SECTOR

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TOTAL INCREASE IN LOANS OUTSTANDING AVAILABLE TO THE  
MANUFACTURING SECTOR BY MATURITY  
(W million)

	1974		1975		1976		1977		1978		1979	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
<u>Short-term Loans</u>												
Commercial banks	443,676	82.9	237,506	74.0	236,422	78.9	553,586	82.7	1,091,410	85.2	879,794	70.2
Savings institutions <u>/a</u>	-	-	-	-	-	-	-	-	-	-	-	-
KDB	13,741	2.6	5,631	1.8	12,780	4.3	23,315	4.2	2,778	0.2	115,957	9.3
KDFC <u>/b</u>	-	-	-	-	-	-	-	-	-	-	-	-
SMIB	24,978	4.7	18,192	5.6	29,231	9.8	44,891	6.7	64,907	5.1	133,362	10.6
CNB	10,434	1.9	7,786	2.4	9,365	3.1	8,748	1.3	3,827	0.3	30,911	2.4
KEB	42,248	7.9	51,943	16.2	7,670	2.6	22,086	3.3	112,288	8.8	88,480	7.1
Eximbank <u>/b, /c</u>	-	-	-	-	4,014	1.3	12,307	1.8	5,281	0.4	4,672	0.4
Life insurance companies	-	-	-	-	-	-	-	-	-	-	n.a.	-
General insurance companies	-	-	-	-	-	-	-	-	-	-	n.a.	-
Subtotal	<u>535,077</u>	<u>100.0</u>	<u>321,058</u>	<u>100.0</u>	<u>299,482</u>	<u>100.0</u>	<u>669,933</u>	<u>100.0</u>	<u>1,280,491</u>	<u>100.0</u>	<u>1,253,176</u>	<u>100.0</u>
<u>Long-term Loans</u>												
Commercial banks	32,918	29.1	49,832	31.4	164,319	55.1	18,005	6.4	124,011	21.0	388,247	36.4
Savings institutions <u>/a</u>	n.a.	-	n.a.	-	40	-	66	-	24	-	-	-
KDB	25,521	22.6	46,432	29.3	77,798	26.1	119,901	42.8	195,569	33.1	297,834	27.9
KDFC <u>/b</u>	16,333	14.5	8,964	5.7	26,766	9.0	23,738	8.5	45,736	7.7	43,681	4.1
SMIB	14,285	12.6	10,513	6.4	14,894	5.0	21,880	7.8	61,657	10.4	69,283	6.5
CNB	662	0.6	-275	-0.2	-707	-0.2	8,783	3.1	2,042	0.3	957	0.1
KEB	20,402	18.1	33,070	20.9	-3,079	-1.0	20,848	7.5	73,037	12.4	209,617	19.6
Eximbank <u>/b, /c</u>	-	-	-	-	-	-	27,280	9.7	70,618	12.0	57,157	5.4
Life insurance companies	2,099	1.9	6,502	4.1	9,739	3.2	36,079	12.9	18,110	3.1	n.a.	-
General insurance companies	674	0.6	3,813	2.4	8,310	2.8	3,744	1.3	-95	-	n.a.	-
Subtotal	<u>112,894</u>	<u>100.0</u>	<u>158,491</u>	<u>100.0</u>	<u>298,080</u>	<u>100.0</u>	<u>289,324</u>	<u>100.0</u>	<u>590,709</u>	<u>100.0</u>	<u>1,066,776</u>	<u>100.0</u>
Total	<u>647,971</u>	<u>100.0</u>	<u>479,549</u>	<u>100.0</u>	<u>597,562</u>	<u>100.0</u>	<u>950,257</u>	<u>100.0</u>	<u>1,871,200</u>	<u>100.0</u>	<u>2,319,952</u>	<u>100.0</u>
of which short-term loans	535,077	82.6	321,058	66.9	299,482	50.1	669,933	70.5	1,280,491	68.4	1,253,176	54.0
long-term loans	112,894	17.4	158,491	33.1	298,080	49.9	289,324	29.5	590,709	31.6	1,066,776	46.0

/a Only the trust account of the Bank of Seoul and Trust Co.

/b On disbursement basis.

/c The Eximbank was established in 1976.

Source: Bank of Korea, KDFC, Eximbank and Korea Insurance Corporation:  
Insurance Statistics Yearbook, 1973-78.

AEP Projects Department  
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ANNEX A  
Table 1

TOTAL INCREASE IN LOANS OUTSTANDING AVAILABLE TO THE  
MANUFACTURING SECTOR BY INSTITUTIONS  
(W million)

	1974		1975		1976		1977		1978		1979	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Commercial banks	476,594	73.4	287,338	59.9	400,741	67.1	571,591	60.2	1,215,421	65.0	1,268,041	54.7
Savings institutions <u>/a</u>	n.a.	-	n.a.	-	40	-	66	-	24	-	55	-
KDB	39,262	6.1	52,063	10.9	90,578	15.1	148,216	15.6	198,347	10.6	413,791	17.8
KDFC	16,333	2.5	8,964	1.9	26,766	4.5	23,738	2.5	45,736	2.4	43,681	1.9
SMIB	39,263	6.1	28,345	5.9	44,125	7.4	66,771	7.0	126,564	6.8	202,645	8.7
CNB	11,096	1.7	7,511	1.6	8,658	1.4	17,531	1.8	5,869	0.3	31,868	1.4
KEB	62,650	9.7	85,013	17.7	4,591	0.8	42,934	4.5	185,325	9.9	298,097	12.8
Eximbank <u>/b,/c</u>	-	-	-	-	4,014	0.7	39,587	4.2	75,899	4.0	61,829	2.7
Life insurance companies	2,099	0.3	6,502	1.3	9,739	1.6	36,079	3.8	18,110	1.0	n.a.	-
General insurance companies	674	0.1	3,813	0.8	8,310	1.4	3,744	0.4	-95	-	n.a.	-
<u>Total</u>	<u>647,971</u>	<u>100.0</u>	<u>479,549</u>	<u>100.0</u>	<u>507,562</u>	<u>100.0</u>	<u>950,257</u>	<u>100.0</u>	<u>1,871,200</u>	<u>100.0</u>	<u>2,320,007</u>	<u>100.0</u>
(US\$ million equivalent)	1,336		989		1,232		1,959		3,858		4,784	

/a Only the trust account of the Bank of Seoul and Trust Co.

/b On disbursement basis.

/c The Eximbank was established in 1976.

Source: Bank of Korea, KDFC, Eximbank and Korea Insurance Corporation: Insurance Statistics Yearbook, 1973-78.

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STRUCTURE OF FINANCIAL SYSTEM  
(in billion won)

	1975		1979		Average annual rate of growth 1975-79 (% p.a. in constant 1975 prices)/b
	Total assets	/a %	Total assets	/a %	
<b>A. Monetary System</b>	10,793.9	76.8	34,539.7	73.8	12.6
1. The Bank of Korea	2,173.7	15.5	5,778.3	12.4	7.5
2. Commercial Banking System	8,620.2	61.3	28,761.4	61.5	13.8
a. Commercial Banks	5,302.3	37.7	18,172.1	38.8	14.7
(i) 5 nationwide commercial banks	4,381.5	31.1	14,722.6	31.5	14.1
(ii) 10 local banks	661.0	4.7	1,917.4	4.1	9.9
(iii) Branches of foreign banks	259.8	1.8	1,532.1	3.3	31.2
b. Specialized Banks	3,317.6	23.6	10,589.3	22.6	12.6
(i) Korea Exchange Bank	1,927.3	13.7	5,557.0	11.9	9.7
(ii) Small-Medium Industry Bank	287.7	2.0	1,049.6	2.2	16.4
(iii) Citizens National Bank	265.7	1.9	1,181.6	2.5	18.7
(iv) Korea Housing Bank	167.7	1.2	838.7	1.8	25.9
(v) Credit sector of agricultural cooperatives	608.3	4.3	1,743.3	3.7	9.6
(vi) Credit sector of fisheries cooperatives	60.9	0.4	228.1	0.5	17.1
<b>B. Nonbank Financial Institutions</b>	3,264.6	23.2	12,239.3	26.2	17.2
1. Development Banks	2,381.5	16.9	7,160.3	15.3	10.9
a. Korea Development Bank	2,328.5	16.6	6,624.0	14.2	9.4
b. Korea Development Finance Corp.	53.0	0.4	212.0	0.5	-
c. Korea Export-Import Bank	-	-	324.3	6.9	-
d. Land Bank /c	-	-	-	-	-
2. Trust Accounts	244.4	1.7	1,229.7	2.6	26.1
3. Insurance Companies	206.7	1.5	1,128.8	2.4	28.7
a. Life insurance companies	105.4	0.7	688.2	1.5	34.4
b. Non-life insurance companies	101.3	0.7	440.6	0.9	21.6
4. Short-term Finance Companies	221.7	1.6	931.2	2.0	20.6
5. Mutual Savings and Finance Companies	63.7	0.3	360.5	0.8	29.9
6. Postal Savings Accounts	47.0	0.3	18.5	0.0	-35.5
7. Securities Firms	99.6	0.7	1,410.3	3.0	63.3
a. Korea Securities Finance Corp.	26.9	0.2	95.1	0.2	15.4
b. Securities dealers & brokers (net)	55.2	0.4	794.1	1.7	64.0
c. Investment trust companies (net)	17.5	0.1	521.1	1.1	96.7
<b>Total</b>	<b>14,058.5</b>	<b>100.0</b>	<b>46,779.0</b>	<b>100.0</b>	<b>13.7</b>

/a In current prices.

/b GNP deflator (1975 = 100) used to derive real values.

/c Korea Land Development Corporation.

Source: BOK and Financial Sector Report.

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ASSETS AND LIABILITIES COMPOSITION OF COMMERCIAL BANKS  
(In percentage)

	1970	1971	1972	1973	1974	1975	1976	1977	1978
<u>Assets</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
Cash and other cash items	3.2	4.6	5.3	4.8	4.5	4.9	5.5	8.8	12.1
Due from BOK & other banks <u>/a</u>	19.4	9.1	20.5	22.4	16.4	19.8	18.3	15.5	11.7
Investments	3.7	4.0	5.0	5.4	4.0	3.9	5.0	6.1	4.7
Loans and discounts	60.6	62.5	52.7	52.0	56.4	48.7	49.8	46.8	46.2
Foreign currency loans	1.4	1.5	1.2	2.3	3.0	4.7	4.1	5.4	8.8
Foreign assets <u>/b</u>	3.7	6.6	5.8	4.4	9.0	12.4	11.1	11.8	11.0
Other assets <u>/c</u>	8.0	11.7	9.5	8.7	6.7	5.6	6.2	5.6	5.5
<u>Liabilities</u>									
Demand deposits <u>/d</u>	18.7	18.8	21.0	19.9	16.2	15.0	16.0	21.0	21.4
Time and savings deposits	52.4	51.3	43.8	43.4	36.2	35.3	36.1	33.8	32.9
Foreign currency deposits	1.1	1.4	0.8	0.9	1.3	7.5	7.6	8.2	5.9
Borrowings from BOK	10.8	9.9	10.5	11.4	17.8	12.6	10.7	8.5	10.7
Net guarantee liabilities <u>/e</u>	2.2	3.1	3.4	5.9	4.3	5.1	5.4	3.9	2.6
Other domestic liabilities <u>/f</u>	5.9	5.1	11.9	8.9	8.3	7.8	9.2	9.4	10.1
Other foreign liabilities <u>/g</u>	4.4	4.5	3.8	3.5	10.4	10.9	8.9	10.6	12.2
Capital reserves	4.5	5.9	4.8	6.1	5.5	5.8	6.1	4.6	4.2

/a Includes special debt of BOK from 1972 and due from NIF from 1975.

/b Includes due from banks in foreign currency.

/c Includes real estate and other assets.

/d Includes interbank deposits.

/e Acceptances and guarantees which appear on both sides of the balance sheet have been netted out.

/f Includes borrowings from trust accounts, treasury agencies, bills payable and special financial debentures issued by banks to BOK from 1972.

/g Includes borrowings in foreign currency by domestic banks and inter alia office borrowings by branches of foreign banks.

ANNEX A  
Table 4

OTHER SOURCES OF FUNDS AVAILABLE TO THE MANUFACTURING SECTOR  
(US\$ million)

	1974		1975		1976		1977		1978		1979	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
<u>Long-term Funds</u>												
<u>Domestic Currency</u>												
Stock	54.1	6.8	113.8	9.9	205.1	13.4	147.6	6.9	290.9	8.2	339.4	11.8
Corporate bonds	54.5	6.8	65.6	5.7	164.4	10.8	289.1	13.5	496.9	14.1	959.2	33.4
Subtotal	<u>108.5</u>	<u>13.6</u>	<u>179.4</u>	<u>15.6</u>	<u>369.6</u>	<u>24.2</u>	<u>436.7</u>	<u>20.4</u>	<u>787.8</u>	<u>22.3</u>	<u>1,298.6</u>	<u>45.2</u>
(W million)/a			(87,014)		(179,271)		(211,784)		(382,073)		(629,859)	
<u>Foreign Currency</u>												
Direct foreign investment	/b	-	/b	-	/b	-	36.4	1.7	76.7	2.2	124.3	4.3
Official loans	20.8	2.6	39.3	3.4	15.9	1.0	16.6	0.8	23.4	0.6	25.0	0.8
Commercial loans /c	415.6	52.2	537.9	46.7	631.0	41.3	892.5	41.6	1,307.3	37.0	440.0	15.3
Cash loans /d	100.6	12.7	109.7	9.5	124.5	8.2	416.9	19.4	858.8	24.3	465.0	16.2
Trade credit /d	150.3	18.9	284.8	24.8	385.6	25.3	344.9	16.1	480.1	13.6	522.4	18.2
Subtotal	<u>687.3</u>	<u>86.4</u>	<u>971.7</u>	<u>84.4</u>	<u>1,157.0</u>	<u>75.8</u>	<u>1,707.3</u>	<u>79.6</u>	<u>2,746.3</u>	<u>77.7</u>	<u>1,576.7</u>	<u>54.8</u>
(W billion)/a			(470.3)		(560.0)		(826.3)		(1,329.2)		(764.7)	
Total	<u>795.8</u>	<u>100.0</u>	<u>1,115.1</u>	<u>100.0</u>	<u>1,526.6</u>	<u>100.0</u>	<u>2,144.0</u>	<u>100.0</u>	<u>3,534.1</u>	<u>100.0</u>	<u>2,875.3</u>	<u>100.0</u>

/a Exchange rate used US\$1 = W 485 for 1975-79.

/b Direct investment to the manufacturing sector for the period 1972-76 amounted to US\$1.7 million.

/c By corporate borrowers; excludes loans channelled through financial intermediaries.

/d Long term portion.

Source: BOK and the Securities Supervisory Board of Korea.

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SUBSIDIZED CREDITS OUTSTANDING FROM DEPOSIT MONEY BANKS TO THE  
MANUFACTURING SECTOR, 1975-79  
(US\$ million)

	1975		1976		1977		1978		1979	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
<u>Loans with Banking Funds</u>										
Export loans	338.9	58.6	461.8	56.9	567.3	56.3	883.2	61.6	1,227.2	67.4
Machine industry promotion /a	23.1	4.0	31.5	3.9	28.2	2.8	26.1	1.8	15.1	0.8
Equipment for export industries	61.2	10.6	76.9	9.4	70.9	7.0	57.0	4.0	42.7	2.3
Special equipment	25.2	4.4	37.2	4.5	36.8	3.6	35.0	2.5	30.1	1.6
Industrial rationalization	14.9	2.6	10.6	1.3	7.1	0.7	7.8	0.5	7.5	0.4
Other /b	4.0	0.7	8.5	1.0	19.0	1.9	19.0	1.3	-	-
<u>Total</u>	<u>467.3</u>	<u>80.7</u>	<u>626.5</u>	<u>77.0</u>	<u>728.7</u>	<u>72.3</u>	<u>1,028.1</u>	<u>71.7</u>	<u>1,322.6</u>	<u>72.5</u>
<u>Loans with Government Funds</u>										
Medium industry	12.7	2.2	9.1	1.1	8.0	0.8	8.8	0.6	9.2	0.5
Foreign loan funds	45.1	7.8	57.0	7.0	75.0	7.4	108.9	7.6	130.2	7.1
<u>Total</u>	<u>57.8</u>	<u>10.0</u>	<u>66.1</u>	<u>8.1</u>	<u>83.0</u>	<u>8.2</u>	<u>117.7</u>	<u>8.2</u>	<u>139.4</u>	<u>7.6</u>
Loans with NIF Funds /c	53.4	9.2	121.0	14.9	196.7	19.5	287.7	20.1	362.7	19.9
<u>Total Subsidized Credits</u>	<u>578.5</u>	<u>100.0</u>	<u>813.6</u>	<u>100.0</u>	<u>1,008.4</u>	<u>100.0</u>	<u>1,433.5</u>	<u>100.0</u>	<u>1,824.7</u>	<u>100.0</u>
Total subsidized credits to manufacturing as a proportion (%) of total loans & discounts		19.9		21.8		21.4		21.0		

/a The Machine Industry Promotion Fund is being phased out and replaced by NIF.

/b Comprises the rural industry and defense industry promotion funds.

/c Loans with NIF are primarily directed to industry.

Source: BOK and the Securities Supervisory Board of Korea.

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TOTAL INCREASE IN LOANS OUTSTANDING AVAILABLE TO THE  
MANUFACTURING SECTOR BY DOMESTIC AND FOREIGN CURRENCY  
(W million)

	1974		1975		1976		1977		1978		1979	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
<u>In Domestic Currency</u>												
Commercial banks	437,977	78.1	191,045	60.7	382,222	68.9	426,111	58.8	757,730	64.5	959,257	64.0
Savings institutions /a	-	-	-	-	40	-	66	-	24	-	55	-
KDB	32,980	5.9	43,733	13.9	76,086	13.7	124,501	17.2	166,611	14.2	172,435	11.5
KDFC /b	1,720	0.3	992	0.3	1,534	0.3	1,507	0.2	3,904	0.3	4,417	0.3
SMIB	39,263	7.0	26,939	8.6	43,935	7.9	63,717	8.8	115,478	9.8	192,442	12.9
CNB	11,096	2.0	7,511	2.4	8,658	1.6	17,531	2.4	5,869	0.5	31,868	2.1
KEB	34,590	6.2	33,893	10.8	20,779	3.7	30,338	4.2	64,086	5.5	98,886	6.6
Eximbank /b,/c	-	-	-	-	3,336	0.6	20,723	2.9	42,850	3.7	39,192	2.6
Life insurance companies	2,099	0.4	6,502	2.1	9,739	1.8	36,079	5.0	18,110	1.5	n.a.	-
General insurance companies	674	0.1	3,813	1.2	8,310	1.5	3,744	0.5	-95	-	n.a.	-
Subtotal	<u>560,399</u>	<u>100.0</u>	<u>314,428</u>	<u>100.0</u>	<u>554,639</u>	<u>100.0</u>	<u>724,317</u>	<u>100.0</u>	<u>1,174,557</u>	<u>100.0</u>	<u>1,498,552</u>	<u>100.0</u>
<u>In Foreign Currency</u>												
Commercial banks	38,617	44.1	96,293	58.3	18,519	43.1	145,480	64.4	457,701	65.7	308,784	37.6
Savings institutions /a	-	-	-	-	-	-	-	-	-	-	-	-
KDB	6,282	7.2	8,330	5.0	14,492	33.8	23,715	10.5	31,736	4.6	241,356	29.4
KDFC /b	14,613	16.7	7,972	4.8	25,232	58.8	22,231	9.8	41,832	6.0	39,264	4.8
SMIB	-	-	1,406	0.9	190	0.4	3,054	1.4	11,086	1.6	10,203	1.2
CNB	-	-	-	-	-	-	-	-	-	-	-	-
KEB	28,060	32.0	51,120	31.0	-16,188	-37.7	12,596	5.6	121,239	17.4	199,211	24.2
Eximbank /b,/c	-	-	-	-	678	1.6	18,864	8.3	33,049	4.7	22,637	2.8
Life insurance companies	-	-	-	-	-	-	-	-	-	-	n.a.	-
General insurance companies	-	-	-	-	-	-	-	-	-	-	n.a.	-
Subtotal	<u>87,572</u>	<u>100.0</u>	<u>165,121</u>	<u>100.0</u>	<u>43,923</u>	<u>100.0</u>	<u>225,940</u>	<u>100.0</u>	<u>696,643</u>	<u>100.0</u>	<u>821,455</u>	<u>100.0</u>
Total	<u>647,971</u>	<u>100.0</u>	<u>479,549</u>	<u>100.0</u>	<u>597,562</u>	<u>100.0</u>	<u>950,257</u>	<u>100.0</u>	<u>1,871,200</u>	<u>100.0</u>	<u>2,320,007</u>	<u>100.0</u>
of which domestic currency	560,399	86.5	314,428	65.6	554,639	92.8	724,317	76.2	1,174,557	62.8	1,498,552	64.6
foreign currency	87,572	13.5	165,121	34.4	42,923	7.2	225,940	23.8	696,643	37.2	821,455	35.4

/a Only the trust account of the Bank of Seoul and Trust Co.

/b On disbursement basis.

/c The Eximbank was established in 1976.

Source: Bank of Korea, KDFC, Eximbank and Korea Insurance Corporation:  
Insurance Statistics Yearbook, 1973-78.

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INTEREST RATE STRUCTURE  
(In percent p.a.)

	Previous rate	January 12, 1980 rate
<u>A. Interest Rates on Deposits</u>		
1. <u>Time Deposits</u>		
Over 3 months	15.0	19.2
Over 6 months	17.1	21.3
Over 1 year	18.6	24.0
2. <u>Installment Savings</u>		
Over 1 year	16.2	20.6
Over 2 years	17.2	22.6
Over 3 years	18.2	25.0
3. <u>Wage Earners Savings Scheme /a</u>		
Over 2 years	25.7 (14.2)	28.4 (16.9)
Over 3 years	27.5 (15.2)	30.9 (18.6)
Over 5 years	30.2 (17.2)	33.6 (20.6)
<u>B. Lending Rates</u>		
	<u>I. Commercial Banks</u>	
1. <u>Working Capital Loans</u>		
Prime borrower	18.5	24.5
Nonprime borrower	19.0	25.0
2. <u>Commercial Notes</u>		
Prime borrower	18.5	24.5
Nonprime borrower	19.0	25.0
3. <u>Overdraft</u>		
Prime borrower	20.5	26.5
Nonprime borrower	21.0	27.0
4. <u>Equipment Loans</u>		
Less than 3 years:		
Prime borrower	18.5	24.5
Nonprime borrower	19.0	25.0
3 to 8 years:		
Prime borrower	19.5	25.5
Nonprime borrower	20.0	26.0
Above 8 years:		
Prime borrower	20.5	26.5
Nonprime borrower	21.0	27.0



	Previous rate	January 12, 1980 rate
5. <u>Export Financing</u>	9.0	12.0
6. <u>National Investment Fund</u>		
Less than 3 years	15.0	21.0
3 to 8 years	16.0	22.0
7. <u>Raw Material Imports for Export     Industries</u>	15.0-16.0	21.0

## II. Korea Development Bank

1. <u>Working Capital Loans</u>		
Government resources	15.0	n.a.
Internal resources:		
Machine Industry Promotion	15.0	21.0
Special Equipment Funds	15.0	21.0
Prime borrowers (standard)	18.5	24.5
Nonprime borrowers (standard)	19.0	25.0
Foreign Commercial Funds <u>/b</u>	12.0-15.5	12.0-15.5/ <u>c</u>
2. <u>National Investment Fund</u>		
Less than 3 years	15.0	21.0
3 to 8 years	16.0	22.0
3. <u>Tourism Development Fund</u>	9.0	n.a.
4. <u>Industrial Rationalization Fund</u>		
Direct lending: Less than 3 years	15.0	21.0
3 to 8 years	16.0	22.0
Through other banks: Less than 3 years	13.5	19.5
3 to 8 years	14.5	20.5
5. <u>Budgetary Resources</u>	7.5-13.5	n.a.
6. <u>Equipment Loans</u>		
Government resources	15.0	n.a.

	Previous rate	January 12, 1980 rate
6. <u>Equipment Loans</u> (Cont.d)		
Government Resources	15.0	n.a.
Internal resources:		
Machine industry promotion -		
Less than 3 years	15.0	21.0
3 to 8 years	16.0	22.0
Over 8 years	17.0	23.0
Special equipment -		
Less than 3 years	15.0	21.0
3 to 8 years	16.0	22.0
Priority industries -		
Less than 3 years	15.0	21.0
3 to 8 years	16.0	22.0
Over 8 years	17.0	23.0
Nonpriority - Less than 3 years	18.5	24.5
3 to 8 years	19.5	25.5
Over 8 years	20.5	26.5
Foreign Commercial Funds <u>/b</u>	12.0-15.5	12.0-15.5/ <u>c</u>
Foreign Currency Loans		
KfW (4th loan)	9.0	9.0
ADB (5th loan)	9.65	9.65
IBRD (2nd loan)	10.5	10.5
(3rd loan)	9.5	9.5
Foreign Commercial Funds <u>/d</u>		
Under 3 years		LIBOR + 1.0%
3 to 7 years		LIBOR + 1.125%
Over 7 years		LIBOR + 1.25%

	Previous rate	January 12, 1980 rate
III. <u>Korea Development Finance Corporation</u>		
1. <u>Domestic Currency Equipment Loans</u> /d		
Loans	20.5	26.0
Debenture subscription	23.0	28.0
Convertible debenture subscription	22.0	27.0
2. <u>Foreign Currency Loans</u>		
IBRD (7th loan)	9.35	9.35
ADB (3rd loan)	9.6	9.6
Commercial loan	Borrowing cost + 1.25%	Borrowing cost + 1.25%

/a Figures in parentheses show the basic interest rate payable by financial institutions; the remainder is subsidized by Government.

/b Converted into domestic currency.

/c Applicable rate determined monthly by KDB's International Department, subject to a ceiling of 21% for priority industries and 24.5% for non-priority.

/d No surcharge for loans extended with bank guarantee; add 0.5% surcharge for collateralized with mortgage.

AEP Projects Department  
July 1, 1980

KOREA

THE KOREA DEVELOPMENT BANK

ANNEX B: REVIEW OF INSTITUTIONAL, OPERATIONAL  
AND FINANCIAL ASPECTS

AEP Projects Department  
September 1, 1980

KOREA

THE KOREA DEVELOPMENT BANK

ANNEX B: REVIEW OF INSTITUTIONAL, OPERATIONAL AND FINANCIAL ASPECTS

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Organization Chart as of March 1, 1980

KOREA

THE KOREA DEVELOPMENT BANK

1. KDB's ROLE IN THE ECONOMY

KDB in Perspective

1.01 KDB is, by far, the largest financial institution in Korea. Its outstanding loan portfolio reached W 2,138 billion (\$4.41 billion) as of December 31, 1979, or 19.2% of total institutional credit outstanding at end-1979. KDB's outstanding guarantee portfolio amounted to \$7.4 billion. Disbursements for loans and investments in 1979 represented about 10.5% of total gross fixed capital formation in Korea during the year.

1.02 KDB's operations encompass (a) domestic and foreign currency lending; (b) equity investments; and (c) issuance of loan guarantees. In 1979, loan commitments totalled W 956 billion (\$1.97 billion) with 79% in domestic currency and the balance in foreign currency; a ratio of 78:22 reflected the split between equipment and working capital financing. New investments in equity and debentures amounted to W 35.9 billion (\$74 million) and new guarantees W 1,142 billion (\$2.35 billion). KDB's clients fall into three major categories: large public sector enterprises in the energy, transportation, social infrastructure and manufacturing sectors;<sup>/1</sup> large private industrial conglomerates such as Dae Woo Heavy Industries and Sam Sung whose capital requirements are so large that only KDB, among the development banking institutions in Korea, can accommodate their needs;<sup>/2</sup> and finally, a more diversified clientele consisting of relatively large-sized private enterprises. The first two categories of borrowers account for a large share of KDB's loan portfolio although the number of enterprises is small.<sup>/3</sup> KDB's clients are often associated with smaller firms through subcontracting arrangements. But only large enterprises, employing more than 300 workers and with assets of more than W 500 million are eligible for financial assistance by KDB. Financial assistance to smaller enterprises is supplied by the Small and Medium Industry Bank (SMIB) and the Citizens National Bank (CNB).

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<sup>/1</sup> Public enterprises (62 companies) accounted for 47.7% of KDB's outstanding loan portfolio at end-1979; 4 companies alone accounted for 34% of KDB's portfolio.

<sup>/2</sup> Loans to five large private companies accounted for 11% of KDB's portfolio at end-1979.

<sup>/2</sup> About 2% of KDB's borrowers (public [4] and private [5]) account for 45% of its portfolio, while 98% by number account for the remainder.

### KDB's Role in the Government's Industrial Strategy

1.03 KDB plays an important role within the framework of the Government's development strategy, as the executing arm of the Government's industrial policies. KDB's Research Department also carries out special studies of industry at the Government's request.

1.04 KDB as Executing Arm of the Government. In accordance with its charter, KDB provides financing to priority industrial projects in conformity with government policies. KDB's support of government objectives is embodied in an annual Operational Program which incorporates sectoral lending targets and earmarks financing for specific projects sponsored by the Government. In addition to allocating the resources it raises independently from the Government, KDB also operates as a conduit for channelling budgetary allocation and special government funding programs /1 to specific projects of national importance, such as Korea Electric Company (KECO), Korea National Railroad or Pohang Integrated Iron and Steel Company. In 1979, KDB received W 83.3 billion in budgetary allocations from the Government representing 7.5% of the Government's capital expenditures for the year. It also received W 310.8 billion from the NIF, representing about 67.9% of total NIF allocations in 1979. The above two sources together constituted about 35% of the total resources raised by KDB in 1979. KDB allocates these resources, as well as the funds it raises independently, in accordance with government priorities. The priority order in KDB's 1980 Operational Program was: (a) government projects for which budgetary funds had been earmarked; (b) equipment financing for priority industries as defined in the KDB Act, i.e. power, coal, iron and steel, air and marine transportation; (c) equipment financing in heavy industry and chemicals; and (d) equipment financing in other industries, and (e) working capital.

1.05 Input into Government Industrial Policies. KDB has helped formulate government policies in the industrial and financial sectors by assisting in government-sponsored studies and participating in a number of consultative groups sponsored by the Government. KDB carries out research studies, which are often used by the Government as an input in formulating industrial plans and policies. In 1977, KDB started a major study on industrial rationalization in Korea. The study considered the mix of industrial policies needed to sustain economic growth as Korea becomes a more open economy. The study covered 27 industrial sectors and used a number of cross country comparators. Studies undertaken in 1978 included a review of policies for overseas investment, a proposal for improved management efficiency in banking institutions, and an analysis of the impact of the value added tax on different income groups. In 1979, KDB carried out

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/1 Particularly the National Investment Fund (NIF) program described in Annex C.



surveys of promotional measures for the machinery industry; of the economic impact of foreign-investment in Korea, and of the benefits of import liberalization for selected items.

1.06 Since its establishment in 1954, KDB has been actively involved in the preparation of the industrial sector's Five-Year Plans. KDB relies on its Research Department to conduct these surveys. Committees on which KDB is represented include the Economic Cabinet Committee, the Foreign Capital Inducement Deliberation Committee, the Advisory Committee for Economic Planning, and the NIF Management Council.

#### Economic Impact of KDB's Lending

1.07 Scale of Output and Value-added. In 1979, KDB approved 703 projects with a total cost of W 1,431 billion; these investments are expected to generate an incremental annual output of W 2,532 billion and incremental annual value-added of W 461 billion.

1.08 Employment Creation. As of December 31, 1979, KDB's clients employed a total of 1 million persons, 80% in the manufacturing sector. The average cost per job for subprojects financed under the latest Bank loan was about \$35,000. This relatively high cost per job reflects KDB's primary role as a promoter of large capital intensive projects in the priority sectors of power, shipbuilding, basic metals, and machinery. Although KDB finances a high proportion of capital intensive projects, it carefully reviews employment impact in evaluating project merits.

1.09 Export Orientation. Exports by KDB borrowers totalled US\$6.6 billion in 1978 or about 52% of all Korean exports. Exports were expected to account for about 50% of incremental sales of projects financed by KDB in 1978-79.

1.10 Sectoral Distribution. The sectoral distribution of KDB's lending operations is shown in Table 6. The share of capital goods industry in KDB's annual commitments has remained relatively constant over the last three years at around 30%-35%. In 1978, loan commitments to the machinery sector represented 9% of total commitments to the manufacturing sector;<sup>/1</sup> the comparable figure for 1979 was 12%.

1.11 Economic Rate of Return Analysis. Table 8 shows the economic indicators of all the projects financed by KDB under IBRD Loan No. 1574-K0 and economic rates of return (ERR) of projects which received loans exceeding US\$750,000. All projects had ERRs in excess of 10% and 18 exceeded 30%. The weighted average economic rate of return was about 30%.

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<sup>/1</sup> On average, commitments to the manufacturing sector reached about 55% of total loan commitments during last three years.

### Influence on Project Design and Technical Assistance

1.12 KDB's influence on project formulation is often limited since project sponsors approach KDB after basic investment decisions concerning product mix, technologies and location have already been taken. Nevertheless, KDB's appraisal staff does contribute to improving the design of some of the investment proposals. KDB, for instance, encourages companies to locate in industrial estates. When new technologies are considered, KDB staff urge project sponsors to enter into technical collaboration agreements with foreign companies. KDB also provides consulting services to clients facing acute difficulties, and may at times assign some of its staff to help borrowers on a temporary basis.

### Promotional Activities

1.13 In addition to the promotional activities pursued directly through its financing operations, KDB has also made significant contributions to the development of the Korean financial system by helping establish several specialized financial institutions. These include a leasing company, two merchant banks, and two overseas investment bank.

1.14 Korea Industrial Leasing Company, Limited (KILC). KILC was established by KDB as a joint subsidiary in December 1972 and started operations in March 1973. As of December 31, 1979, KILC's paid-in capital was W 3 billion with 50% owned by KDB, 45% by the Manufacturers Hanover Leasing Company and the remaining 5% by the Korea Exchange Bank. KILC's objective is to lease industrial machinery, principally to smaller firms which cannot afford outright purchase. As of December 31, 1979, KILC has written 496 lease contracts amounting to W 79.6 billion. A total of \$17.5 million had been earmarked from previous Bank loans (Nos. 1338-KO and 1574-KO) to KDB for use by KILC. Eligibility was restricted to enterprises with assets of less than W 600 million or projects with a maximum cost per job of \$15,000. Utilization of this component has been satisfactory. As of December 31, 1979, \$17.5 million had been committed and \$14.7 million disbursed.

1.15 Saehan Merchant Banking Corporation (SMBC). KDB was instrumental in establishing SMBC in 1977. SMBC is a joint venture between Korean (50%) and international shareholders (50%). KDB is the largest shareholder with 30% of the W 6 billion equity at end-1979; Samuel and Company held 20.5%. SMBC performs the dual function of mobilizing foreign commercial resources and developing the securities market in Korea.

1.16 Korea Associated Securities Inc. (KASI). KASI is an investment bank registered under the corporate laws of the State of New York. The principal purpose of KASI, which was established in 1977 is to raise foreign currency capital for Korean enterprises and to attract US and other foreign investments in Korea. KDB held 50% of the \$6 million paid-up capital as of December 31, 1979 with the remainder almost equally distributed among six other Korean banks.

1.17 Korea International Merchant Bank (KIMB). KIMB was established in 1979 to raise foreign commercial resources and develop the financial market in Korea. As of December 31, 1979, KDB and the Korea Exchange Bank held respectively 10% and 40% of its W 5 billion share capital. Foreign shareholders held the balance of 50%.

1.18 Korea Associated Finance Ltd. (KAF). KAF was established in Hong Kong in 1979 as a merchant bank. KAF's objective is to raise foreign capital for Korean companies. As of December 31, 1979, KDB held 7.5% of KAF's paid in share capital of \$5 million.

#### Resource Mobilization

1.19 KDB's resource position is analyzed in paras. 4.10 to 4.12. As of December 31, 1979, KDB had total resources short and long-term, of W 2,848 billion equivalent. Borrowings from the NIF remain the single largest source of funds (28.4%) followed by equity with about 17%. In addition to its share capital which is subscribed by the Government, KDB depends for about 45% of its total resources on funds provided by the Government. In recent years, however, KDB succeeded in mobilizing additional resources in its own name to supplement government funding.

1.20 On the domestic currency side, KDB has issued industrial finance debentures (IFD) with a maturity of 2 to 5 years /1 and an aggregate value of W 277 billion since 1975. Outstanding IFDs accounted for about 5.0% of KDB's total resources at end-1979. The present structure of the domestic capital market does not permit KDB to issue bonds with maturities over 5 years. However, KDB's lending for equipment financing would require resources having maturities exceeding eight years. As a result, KDB continues to rely on other sources of long-term domestic currency funds primarily from the Government and the NIF.

1.21 On the foreign currency side, KDB has raised \$1,422 million from commercial sources over the period 1970-79 /2 to supplement the \$492 million obtained from official sources (IBRD, ADB, USAID, and KfW). This success in mobilizing foreign commercial resources is very impressive.

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/1 Of the bonds issued, 48% had a maturity of two years, 50% a maturity of three years and 2% a maturity of five years.

/2 Of which \$1,063 million in 1978-79.

## 2. INSTITUTIONAL ASPECTS

### Legal Framework, Organization and Staff

2.01 Legal Framework and Ownership. KDB was established in 1954 as a wholly government-owned institution to finance the postwar rehabilitation of industry. KDB's operations, broad policy framework, scope of activities, administration and capitalization are governed by the KDB Act. The Act was last amended in December 1977, in part to increase KDB's authorized capital from W 300 billion to W 600 billion. As of December 31, 1979, KDB's paid-in capital was W 331.8 billion.

2.02 Management. In accordance with the KDB Act, the Minister of Finance supervises KDB's operations. A full-time Board of Directors (Appendix 1) comprising the Governor, Deputy Governor and seven Executive Directors, conducts KDB's operations. KDB's Governor is appointed by the President of the Republic on the recommendation of the Minister of Finance; the Deputy Governor and Executive Directors are appointed by the Minister of Finance. The term of office for Board members is three years and is renewable. Mr. Yeung Ki Hah, former President of the Korea First Bank, was appointed Governor of KDB in July 1980. The quality of KDB's senior and middle level management is satisfactory.

2.03 Organization. KDB's head office comprises 21 departments grouped according to broad functions; each group reports to one of the seven Executive Directors. KDB's organization chart is appended. The Head Office is responsible for all projects in the Seoul area. The 10 local branch offices outside the Seoul region have the authority to approve working capital loans; /1 other types of loans are appraised at the branch level and forwarded to the Head Office for further analysis and approval. The branches are also responsible for the supervision of projects in their area. In addition to its domestic branch offices, KDB has representative offices in London, New York, Tokyo, Kuwait, Singapore, Hong Kong and, more recently, in Frankfurt. The main focus of these offices is foreign currency resource mobilization.

2.04 Staff. Table 3 shows the breakdown of KDB's professional staff. Over the past few years KDB's total staff size has not changed significantly. The total number of staff currently stands at 1,961 of whom 584 hold a position of Deputy Manager and above. /2 The quality of KDB's professional staff is satisfactory. Staff turnover for professionals has declined from 14% in 1977 to 5.5% in 1979. In the past, KDB lost some of its better professional staff to other Korean financial institutions and to industry. The reduction in the staff turnover rate in recent years reflects, to an

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/1 W 30 million to W 110 million depending on the branch.

/2 Based on academic and work experience, the number of professionals is 591.

extent, the slowing down in the rate of growth of the Korean economy. KDB continues to attract new recruits of acceptable quality, including college graduates. KDB provides adequate in-house and external training for all its staff. A number of officers are also sent to various financial institutions abroad for further training; in 1979, 73 officers were sent abroad for on-the-job (63) and academic (10) training.

#### Operational Policies

2.05 KDB's operations are governed by the KDB Act and Enforcement Decree, KDB's By-Laws, Operating Manuals and Policy Statement (Appendix 2). KDB has also formulated a Statement of Development Strategy (Appendix 3) for the period 1980/82, highlighting its specific short-run developmental objectives. KDB's Policy Statement incorporates financial prudence guidelines and limits applicable to KDB's equity participation, collateral coverage and total financial assistance to any single enterprise. With respect to equity operations, the Policy Statement stipulates that KDB should not normally make equity investments in excess of either 15% of its own equity or 50% of the paid-in capital of the enterprise. Excluding the Readjustment Corporation, /1 KDB had exceeded these limits in three cases as of December 31, 1979. Its financing to these companies amounted to W 192 billion (58% of KDB's total investment portfolio).

2.06 The Policy Statement also provides that KDB shall not normally extend financial assistance to any single entity in excess of either 25% of its own equity or 65% of the total assets of the enterprise. As of December 31, 1979, KDB had exceeded these limits in 15 cases amounting to W 3,555 billion and representing 57% of KDB's aggregate loan, investment, and guarantee portfolio. /2 The W 3,555 billion portfolio comprised 71% in the form of guarantees, /3 25% in loans and 4% in equity investments. Finally, the Policy Statement provides that KDB shall require a collateral coverage of at least 125% for loans and 120% for guarantees. At end-1979, KDB has exceeded these limits in 21 cases /4 representing about 43% of the outstanding loan portfolio and 63% of the outstanding guarantee portfolio. The large size of the Government-owned and government designated enterprises to which KDB provides financing at government behest accounts for the large proportion of "exceptions" in KDB's portfolio.

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/1 A full subsidiary of KDB in accordance with Article 53 of the KDB Act.

/2 Two companies - Korea Electric Co. and Pohang Iron and Steel Co. - accounted for 68% of exceptions.

/3 95% was covered by the GRA under which the financial risk is transferred to the Government.

/4 KECO AND POSCO accounted for 70% by amount.

### Project Appraisal and Supervision

2.07 Project Appraisal. KDB's appraisal standards and procedures remain satisfactory for projects funded out of its own resources (including foreign official borrowings). The latitude given KDB to exercise its independent judgement is however severely curtailed for project financed out of government resources. KDB undertakes reasonably thorough economic analyses. Economic Rates of Return (ERR) are calculated for projects funded from official borrowings and requiring foreign exchange financing of more than \$750,000 and for all other projects whose cost exceeds W 2 billion. KDB's appraisal analyses also include an assessment of the environmental impact of the projects it finances.

2.08 Project Supervision. KDB's project supervision procedures are generally satisfactory. Follow-up work, however, is not entrusted to a separate department; it is carried out by the loan appraisal officers, either at Headquarters or at the branch level, or jointly. Compliance by clients in fulfilling quarterly reporting requirements is satisfactory. Audited financial statements are required for all foreign currency loans, and for domestic currency loans exceeding W 100 million. KDB frequently assigns its own staff to problem projects to serve in a managerial capacity or appoints a representative on the Board of Directors. Overdue or insufficiently collateralized loans are transferred to the Special Loan Department which works closely with the Business Control Department. Foreclosures are transferred to the Readjustment Corporation.

### Procurement and Disbursement

2.09 KDB's procurement and disbursement procedures are designed to ensure a reasonable degree of competition in procurement and the appropriate use of funds. Procedures were changed in 1978 to include three methods of procurement: international competitive bidding (ICB); limited competitive bidding; and negotiated contracts. ICB is the most frequent and accounted for 56% of all procurement contracts under the third Bank loan. In cases where the estimated procurement is less than \$1 million, limited competitive bidding is followed. Suppliers' bids from at least five countries are required. In 1979, this method accounted for 17% of all procurement contracts. Occasionally, when patent rights, compatibility with existing equipment or unique specifications make it necessary, KDB accepts negotiated contracts with a single supplier. In 1979, 27% of all procurement financed by KDB was made under the negotiated contract method. The final procurement contract is always subject to KDB's approval. Disbursements are monitored and authorized in accordance with progress in project implementation.

### 3. OPERATIONS

#### Scope of Operations

3.01 The KDB Act allows KDB to undertake working capital and equipment financing, issuance of bonds, borrowing of foreign capital, and transactions in foreign exchange. Some of these operations, <sup>/1</sup> however, are restricted to enterprises which have already obtained term loans or guarantees from KDB. The annual volume of KDB's operations is guided by its Operational Program which is subject to approval by the Minister of Finance. The Operational Program sets out quantitative targets for KDB's financing on the basis of available resources.

#### Volume of Operations

3.02 KDB's financing operations fall into three broad categories: (a) lending in foreign and domestic currency for equipment purchases and working capital; (b) investment in equity and corporate bonds and debentures; and (c) issuance of loan guarantees, in foreign and domestic currency. The volume of KDB's operations particularly in domestic currency has often been constrained by the non-availability of sufficient resources. Over the past few years, however, KDB has been able to expand rapidly its foreign commercial borrowings. Conversion of a part of the foreign commercial resources into Won and issuance of domestic currency IFDs have enabled a reasonable growth of domestic lending. KDB's loan, investment and guarantee operations for 1976-79 are shown in Tables 4, 9 and 11 and are summarized as follows:

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<sup>/1</sup> Working capital finance, demand deposits, dealings in foreign exchange.

SUMMARY OF KDB'S OPERATIONS, 1976-79  
(won billion)

	1976	1977	1978	1979
<u>Loan Commitments</u>				
Domestic currency	194.4	304.8	466.2	750.3
Foreign currency	34.1	41.4	121.8	205.4
<u>Total loans</u>	<u>228.5</u>	<u>346.2</u>	<u>588.0</u>	<u>955.7</u>
<u>New Investments</u>				
Equity investments	40.8	63.6	83.3	26.9
Bonds and debentures	4.8	8.2	3.8	9.0
<u>Total investments</u>	<u>45.6</u>	<u>71.8</u>	<u>87.1</u>	<u>35.9</u>
<u>Guarantees Issued</u>				
Domestic currency	35.7	60.8	40.7	68.8
Foreign currency	1,310.8	1,035.6	1,446.6	1,073.7
<u>Total guarantees</u>	<u>1,346.5</u>	<u>1,096.4</u>	<u>1,487.3</u>	<u>1,142.5</u>
<u>Total commitments</u>	<u>1,620.6</u>	<u>1,514.4</u>	<u>2,162.4</u>	<u>2,134.1</u>

3.03 KDB's loan approvals amounted to W 957.8 billion in 1979, an increase of 63% over 1978. Since 1977, domestic currency lending has increased at an annual average rate of 57%, and foreign currency lending at 123%. As a share of KDB's total lending, foreign currency lending has increased from 12% in 1977 to 21% in 1979. Over the past three years, working capital loans averaged 20% of total domestic currency loans. As of December 31, 1979, KDB's outstanding loan portfolio reached W 2,138 billion, more than twice the 1977 level.

Characteristics of Lending Operations

3.04 Tables 5 and 6 show an analysis of loan commitments during 1977-79 and of outstanding loans as of December 31, 1979. Outstanding foreign currency loans have risen from 10.4% of KDB's total loan portfolio at end 1977 to 15.1% at end 1979. The share of the private sector in KDB's outstanding portfolio has also increased from 46.4% at end 1977 to 52.3% at end 1979. New projects accounted for 30% of KDB's commitments in 1979. The average maturity of equipment loans has increased from 6.0 years in 1977 to 7.9 years in 1979; in the case of working capital loans, the average duration has declined from 20 months in 1977 to 13 months in 1979.



3.05 The geographic distribution of loans has remained more or less the same over the last three years with Seoul and Busan, the predominant industrial areas, absorbing about 50% <sup>/1</sup> of all loan commitments in 1977-79. The manufacturing sector accounted for 57.4% of loan commitments in 1979 compared with 60.1% in 1977. The share of capital goods industries has remained relatively constant at 33% over the last three years while the machinery industry accounted for about 8%.

3.06 Loans Made at Government's Behest. KDB extends financial assistance to public sector companies at the behest of the Government, without undertaking independent appraisal. As of December 31, 1979, outstanding loans to such companies amounted to W 721.3 billion <sup>/2</sup> or 34% of KDB's outstanding loan portfolio. Under the second Bank Loan to KDB, the Government agreed to relieve KDB of the financial risks pertaining to such loans.

#### Investment Operations

3.07 Table 9 gives a summary of KDB's investment operations for 1976-79. Total investments approved during 1979 amounted to W 35.9 billion and KDB's investment portfolio stood at W 332.2 billion at end-1979. Equity investments accounted for 90% of the total investment portfolio; the remaining portfolio comprised bonds and debentures.

3.08 As of December 31, 1979, 75% of KDB's outstanding portfolio was invested in public sector companies. Manufacturing industries accounted for 75% of total portfolio (Table 10).

#### Guarantee Operations

3.09 As of December 31, 1979, KDB's guarantee portfolio stood at W 3,722.2 billion (Table 11). About 96% of all outstanding guarantees were in foreign currency. Domestic currency guarantee commitments have increased marginally from 6% in 1977 to 12% in 1979. Guarantees issued to the public sector declined from 42% in 1977 to 30% in 1979. The KDB Act sets a ceiling of 10 times its paid-in capital and reserves on KDB's guarantee operations. As of December 31, 1979, that ratio was 8.1 times its equity.

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<sup>/1</sup> This percentage is somewhat misleading, as it includes substantial lending to KECO whose head office is in Seoul.

<sup>/2</sup> Korea Electric Company - W 536.8 billion; Korea National Railways - W 167.3 billion; Korea Coal Corporation W 11.6 billion; and Korea Highway Corporation - W 5.6 billion.

### Utilization of Bank Loan No. 1574-K0

3.10 As of March 1, 1980, KDB and KILC had committed \$95.6 million and \$9.6 million respectively of the proceeds of the latest IBRD Loan (\$110 million). Disbursements reached \$67.6 million. Table 8 presents an analysis of the subprojects financed under Bank Loan No. 1574-K0. KDB's subloans ranged in size from \$300,000 to \$7.5 million with an average of about \$2.2 million; KILC's average lease amount was \$235,000. As of December 31, 1979, machinery, metal and chemical industries accounted respectively for 19%, 9% and 12% of KDB's total approvals under Bank Loan No. 1574-K0. KDB contributed about 43% of total project costs. The 43 projects financed by KDB under this loan are expected to generate export sales of \$292 million and to create 6,700 new jobs at an average cost per job of about \$35,000. Financial rates of return range from 10% to 37% with an average of 22%; the average ERR is about 30%.

## 4. FINANCIAL CONDITION, PERFORMANCE AND RESOURCE POSITION

### Financial Condition

4.01 Assets. KDB's asset base has been growing at an average of 37% p.a. during the period 1977-79. Total assets reached W 2,869 billion (\$5.9 billion) at end-1979. Over the period 1977-79 the shares of KDB's loan and investment portfolios in total assets averaged 72.3% and 14.5% respectively.

4.02 Liabilities and Equity. As of December 31, 1979, KDB's total assets were financed by short-term debts (12.1%), long-term liabilities (70.8%) and equity (17.1%). KDB's equity base has declined in relative terms from 25.7% at end-1977. Foreign currency borrowings have increased from about 24% of outstanding long-term resources in 1977 to 40% in 1979 as a result mainly of KDB's success in raising foreign commercial funds.

4.03 Liquidity Position. As of December 31, 1979, the current ratio stood at 1.8:1 as against 1.2:1 at end-1978; this improvement, however, is due to a different presentation of the balance sheet in 1979. KDB's debt service ratio is satisfactory and amounted to 1.3 in 1979 as against 1.4 in 1978.

4.04 Debt/Equity Ratio. The KDB Act limits KDB's outstanding guarantees and IFDs to ten times its equity; as of December 31, 1979, the ratio stood at 8.1. The long-term debt/equity ratio stood at 6.3:1 at end-1979, and was well within the contractual limit set with the Bank at 10:1./1

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/1 The original 5:1 limit was increased in July 1979 to 10:1.

### Financial Performance

4.05 Table 16 shows KDB's financial performance between 1976 and 1979. KDB's gross interest spread has declined from 3.9% in 1977 to 3.0% in 1979, and its administrative expenses have increased marginally <sup>/1</sup> from 0.7% of average total assets in 1978 to 1.0% in 1979. As a consequence, KDB's net income to average total assets declined from 2.2% in 1976 to 1.5% in 1979. Since the Government made no additional capital contribution in 1979, the return on KDB's average net worth increased from 7.5% in 1978 to 7.9% in 1979.

### Portfolio Quality

4.06 Loan Portfolio. Tables 17 and 18 show the status of KDB's portfolio for the years 1976-79. KDB's arrears situation, although still satisfactory, has deteriorated in 1979 owing to the recession which affected the economy as a whole and the tight monetary policy enforced by the Government; KDB, however, considers this deterioration to be temporary. As of December 31, 1979, arrears of principal and interest (in excess of three months) reached W 9.8 billion<sup>/2</sup> or approximately 0.5% of the total loan portfolio compared to 0.3% at end-1978. Principal affected by arrears reached 7% of total portfolio at end-1979 as against 2.9% in 1978. The amount of rescheduling relative to the loan portfolio has likewise increased from 3.3% in 1978 to 7.5% in 1979. Total portfolio affected by reschedulings and arrears (over three months) has jumped from 6.2% in 1978 to 14.5% in 1979. On the other hand, transfers to the Readjustment Corporation (RAC), KDB's collection agency, have decreased in 1979. Despite a perceptible deterioration in 1979, KDB's loan portfolio remains reasonably sound, and its collection performance (97.4%) satisfactory.

4.07 Guarantee Portfolio. As of December 31, 1979, KDB's outstanding guarantee portfolio comprised 139 companies for a total of W 3,722.1 billion of which 72.7% was covered under the Government's Guarantee Release Agreement (GRA).<sup>/3</sup> Seven clients, all in the private sector, were in default on guarantees affecting about 1.4% of KDB's guarantee portfolio <sup>/4</sup> compared to 0.2% in 1978. Payments made by KDB in 1979 on defaulted guarantees amounted to W 6.9 billion as against W 2.3 billion in 1978.

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<sup>/1</sup> The increased administrative expenses mainly resulted from an exceptional increase in retirement allowances.

<sup>/2</sup> Data quoted in this paragraph are based on audited accounts and differ substantially from the figures supplied by KDB in Tables 17 and 18.

<sup>/3</sup> Under the GRA, the Government assumes the financial risk for all foreign guarantees issued to government-controlled enterprises and priority enterprises as defined in the KDB Act.

<sup>/4</sup> Of which 59% was covered under the GRA.

4.08 Equity Portfolio. As of December 31, 1979, KDB had outstanding investments of W 300 billion in 37 companies, most of which were operating satisfactorily; only three companies, accounting for 6.2% of total investments, were experiencing losses. The dividend yield on KDB's investment portfolio has increased marginally, but the overall return including capital gains declined from 5.6% in 1978 to 4.5% in 1979. The profitability of KDB's investments is low because of the large share in the portfolio of public and semi-public entities which distribute little or no dividends. However, KDB's equity portfolio is sound.

4.09 Provisions. The government guarantee (GRA) which covers most of KDB's guarantee portfolio is satisfactory and alleviates the need for special provisions. KDB's provisions against its loan and investment portfolio reached only W 300 million at end-1979 or 0.01% of the total outstanding portfolio. The level of provisions made by KDB is based on writeoffs in preceding years. Actual writeoffs can be kept at an artificially low level and this procedure therefore appears inadequate. KDB's financial statements have been audited by Sam Poong Company in 1979. While recognizing that KDB is required by law to set aside special equity reserves to cover exceptional losses, the auditors recommended that KDB set aside additional provisions at 1% of outstanding portfolio. Provisions of W 24.7 billion have been recommended.

#### Resource Position

4.10 KDB's resource position as of December 31, 1979 is shown in Table 19. As of this date, KDB's total resources amounted to W 2,848.7 billion equivalent of which 71% had been mobilized in domestic currency and 29% in foreign currency. By comparison, the currency mix of KDB's outstanding portfolio (loans and investments) at the same date was substantially different since the domestic currency component reached 87% (domestic currency loans and investments) and the foreign currency component reached 13% only. The larger share of domestic currency operations (87% as against 71%) reflected the greater demand for domestic currency funding relative to available domestic currency resources. KDB suffers from insufficient domestic currency resources and to cover this gap, KDB has converted a substantial portion of its foreign commercial resources (approximately 60%) into Won to finance its domestic currency lending.

4.11 As of December 31, 1979, KDB's total uncommitted long-term resources amounted to W 216.2 billion (\$446 million). In addition, available short-term domestic currency resources amounted to W 78 billion. KDB's total loan commitments are projected at about \$1,940 million in 1980, or approximately three times the size of the resources available for commitment at end 1979.

4.12 KDB's principal sources of domestic currency funds are budgetary allocations and borrowings from government funds. Together, these two sources accounted for about 65% of KDB's total long-term domestic resources <sup>/1</sup> as of end-1979. The National Investment Fund (NIF) has become KDB's single largest source accounting for 43.9% of KDB's total long-term domestic funds at end-1979 followed by equity resources with 26.7% and budgetary allocations with 16.9%. Domestic currency long-term resources raised by KDB independently from the Government comprise deposits and Industrial Finance Debentures. These two sources together accounted for less than 8% of KDB's total long-term domestic currency resources at end-1979.

4.13 Industrial Finance Debentures (IFDs) - To augment its domestic currency resources and to stimulate capital market development, KDB issues discount debentures with maturities of one to three years and coupon debentures with a five-year maturity. Issuance of debentures requires the approval of the National Assembly, since the KDB bonds are guaranteed by the Government. KDB's domestic resource constraint has been solved in the past by converting some of KDB's foreign commercial borrowings into domestic currency. A more satisfactory long-term solution lies in the issuance by KDB of increasing amounts of IFDs with a gradual lengthening of maturities. Through end-1979, KDB had raised an aggregate of about W 374 billion through debenture issue; W 143.2 billion were outstanding at end-1979, representing 7.8% of KDB's total long-term domestic resources. The issuance of domestic IFDs has been encouraged by the Korean authorities as a means of lengthening maturities in the capital market. So far, however, KDB has been able to issue five-year debentures in limited amounts only, except in 1977, when they accounted for 8% of the total amount issued. Since the January 1980 upward adjustment of interest rates in Korea, IFDs are issued at nominal interest rates of 17.8% to 21.8% for the one to three-year category and 24% for five year debentures. With prepayment of interest, however, their effective cost to KDB is between 28% and 29%. Given KDB's maximum lending rate of 26.5% for capital loans, the use of these funds implies a loss of about two percentage points. In fact, KDB has been onlending part of its IFD proceeds to priority borrowers at subsidized interest rates (i.e., lower than 26.5%), thus increasing the negative spread.

4.14 Foreign Currency Resources. KDB has been very successful during the past few years in its efforts to supplement its foreign borrowings from official sources with funds raised from commercial sources. Foreign commercial borrowings accounted for about 75% of KDB's total foreign currency resources at end-1979. In 1979 alone, KDB was able to mobilize a total of \$755 million from commercial sources comprising (a) \$43.9 million through the issuance of Euro-Bonds denominated in Kuwaiti Dinar; and (b) two syndicated loans of Yen 28 billion and \$600 million. A \$200 million

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<sup>/1</sup> Excluding funds raised in foreign currency and converted into Won, but including equity resources (i.e., W 1,842 billion).

portion of the latter loan has been temporarily invested in BOK's Monetary Stabilization Bonds. A swap arrangement with BOK gives KDB adequate protection against any foreign exchange risk and allows repurchase of the funds for future lending operations. During 1980, the Government intends to encourage KDB to raise an additional loan of \$600 million from the international capital market.

## 5. PROSPECTS AND RESOURCE REQUIREMENTS

### Operational Projections

5.01 In the past, KDB's growth has been limited by the availability of funds rather than loan demand. As a consequence, KDB usually prepares its operational projections on the basis of the estimated availability of funds. KDB expects its loan operations to increase by 18% in 1980 on an approval basis, and an average of 14% for the 1981-83 period. Higher levels of operations are projected in 1980 following the Won devaluation. Overall, these projections seem rather conservative in light of the 47% growth rate which KDB experienced during 1976-79. The share of foreign currency loans in total commitments is projected to increase to 20% as against 17.5% in the period 1977-79. The projected share of working capital financing at 20% of domestic operations is in line with previous years, but represents a decline from the fairly high level of 27.3% in 1979. The year 1979 was marked by very tight liquidity for Korean firms and an exceptional increase in KDB's lending for working capital. KDB's investment and debenture portfolio is expected to increase annually at the historical rate of 21%. KDB expects to issue guarantees averaging \$ 1.9 billion annually; this would result in an increase in its guarantee portfolio of 10% p.a. over the period 1980-83.

5.02 A summary of KDB's projected operations is shown in Table 21. KDB's total loan commitments are expected to increase from W 955.7 billion in 1979 to W 1,668.4 billion in 1983. The share of domestic currency loans in total commitments would remain unchanged at about 79%. Given KDB's past performance, its projected level of operations appears to be somewhat conservative. However, as in the past, the actual operational level will be largely determined by resource availability.

### Resource Requirements

5.03 To meet its projected commitments, KDB plans to borrow an aggregate of about W 4.8 billion (\$8.2 billion) between 1980 and 1983, of which 63% would be in domestic currency. The lower 63% share of domestic currency resources in total borrowings relative to the 79% share of domestic currency lending in total commitments suggests that KDB will continue to rely on the conversion of foreign commercial borrowings to finance its domestic currency operations. KDB expects budgetary funding and NIF

allocations to remain its principal sources of domestic resources, accounting for about 63% of total domestic currency resource mobilization. Domestic currency IFDs would provide the remainder. KDB's projected borrowing program for 1980-83 is shown in the following table. KDB plans to raise W 1,100 billion through issuance of domestic IFDs over that period.

BORROWING PROGRAM TO MEET COMMITMENTS, 1980-83  
(Won and Dollar Millions)

	1980	1981	1982	1983
<hr/>				
<u>Domestic Currency Borrowings (Won)</u>				
Borrowings from Government	83,222	95,705	110,061	126,570
National Investment Fund	295,900	340,285	391,328	450,027
Industrial Finance				
Debentures (Domestic)	200,000	250,000	300,000	350,000
Subtotal	<u>579,122</u>	<u>685,990</u>	<u>801,389</u>	<u>926,597</u>
<u>Foreign Currency Borrowings (US\$)</u>				
Commercial sources				
(IFDs)	100	100	100	100
(Bank loans)	600	600	600	600
Subtotal	<u>700</u>	<u>700</u>	<u>700</u>	<u>700</u>
Official sources				
(ADB)	-	60	-	-
(IBRD)	100	-	100	-
Subtotal	<u>800</u>	<u>760</u>	<u>800</u>	<u>700</u>
<u>Total Borrowings (Won)</u>	<u>1,043,122</u>	<u>1,126,790</u>	<u>1,265,389</u>	<u>1,332,597</u>

5.04 During the 1980-83 period, KDB intends to raise from official sources only 8.5% of its total \$3.1 billion foreign currency borrowings. The international capital market is expected to supply the remaining 91.5%. The mobilization of this very substantial volume of foreign commercial resources will depend on Korea's continued creditworthiness and conditions in the international capital markets. It will also depend on the amount of foreign commercial funds which KDB is allowed by the Government to raise in any given year, within the framework of overall capital inflows into Korea.

### Financial Forecasts

5.05 KDB's projected income statements, balance sheets, and cash flow statements for the years 1980-83 are shown in Tables 22, 23, and 24. A gradual decline is expected in KDB's gross interest spread from 3.0% in 1979 to 2.4% in 1983; net return on average assets would consequently decline from 1.5% to 1%, a level which KDB considers satisfactory for a government institution. In gross terms, however, KDB's annual net income would increase from W 36.5 billion in 1979 to W 58.0 billion by 1983.

Administrative expenses are projected to remain at the satisfactory level of about 0.9% of average total assets over the projection period. The debt service coverage is also expected to remain satisfactory, not falling below 1.2 times. Total assets are forecast to increase at an average annual growth rate of around 24% and to reach W 6,900 billion (\$11.9 billion) in 1983. A decline is expected in KDB's current ratio from 1.8 to 1:1; the long-term debt/equity ratio, which stood at 6.3:1 the end of 1979, is not expected to exceed 8:2:1 until 1983, still within the contractual limit of 10:1 agreed with the Bank.



KOREA

THE KOREA DEVELOPMENT BANK

Board of Directors  
(as of March 1, 1980)

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Name	Position	Background
<hr/>		
Joon Sung Kim	Governor	Appointed in December 1978. Previously President of the Korea Exchange Bank. Career spent mainly in private enterprises and banking institutions.
Eung Suh Park	Deputy Governor	Appointed in 1978. Joined KDB in 1954. Appointed Director in 1968, Executive Director in 1971, Auditor in 1977.
Duk Hyong Park	Executive Director	Appointed in 1975. Joined KDB in 1942. Appointed Director in 1969.
Yang Sool Chang	Executive Director	Appointed in 1976. Joined KDB in 1948. Appointed Director in 1973.
Baum Sauck Lee	Executive Director	Appointed in 1977. Joined KDB in 1950. Appointed Director in 1970.
Eun Ki Hong	Executive Director	Appointed in 1977. Joined KDB in 1948. Appointed Director in 1973.
Jung Sang Kim	Executive Director	Appointed in 1978. Joined KDB in 1953. Appointed Director in 1974.
Yeong Kon Kim	Executive Director	Appointed in 1978. Joined KDB in 1954. Appointed Director in 1975.
Kyu Hong Kim	Executive Director	Appointed in 1978. Joined KDB in 1954. Appointed Director in 1973.

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AEP Projects Department  
March 15, 1980

KOREA

THE KOREA DEVELOPMENT BANK

Policy Statement

(Approved by Board of Directors on April 4, 1975)

Economic Role of KDB

1. The KDB shall assist in the economic development of Korea in conformity with its purpose as stated in the Korea Development Bank Act (KDB Act) enacted December 30, 1953, as amended, its By-Laws enacted February 16, 1954, as amended, and the other regulations governing its operations.

Operations

2. The KDB will carry out its operations in accordance with sound management and banking principles and practices. It shall endeavor to specialize in extending capital funds to such industries as are designated by the Government's economic plans or decrees as priority industries as well as other major basic industries which form the substructure of the economy. KDB may also make equity investments, provide working capital loans and render managerial and technical assistance to its Borrowers when the need arises. KDB will also extend guarantees on behalf of client enterprises. KDB, however, will not compete with other financial institutions in lending and administering industrial loans to assist major industries.

Project Selection

3. It will finance enterprises which are soundly managed and which appear, on careful economic, financial and engineering investigation to be viable. Following sound banking practices, the projects will be analyzed taking the following factors into consideration before making a commitment of financial assistance: (a) national economic benefits; (b) technical feasibility; (c) financial soundness and profitability; (d) marketability; and (e) quality of management.

Criteria for Selection of Borrowers

4. In its operations, preference will be given to the following major industries:

- (a) Generation, transmission and supply of electricity;
- (b) Coal-mining;
- (c) Ship-building;

- (d) Iron and steel manufacturing;
- (e) Electronics;
- (f) Export industries, designated by the Government to produce export commodities;
- (g) Import-substitution industries and industries producing raw materials necessary for export and import-substitution;
- (h) Indigenous industries and labor intensive industries; and
- (i) Such other industries as may be designated by the Government's economic plans or decrees as priority industries.

Qualifications for Eligible Borrowers

5. Eligible borrowers for KDB financing must meet the following qualifications:

- (a) Borrowers must be financially sound;
- (b) Borrowers must possess management and technical capacity for implementing the projects being financed;
- (c) Borrowers should not have defaulted on any of their outstanding obligations to KDB.

Maximum Investment and Assistance

6. (a) KDB shall not subscribe to and/or underwrite stocks (including investment certificates) if the paid-up amount of the stocks so held by KDB will exceed KDB's own paid-up capital;
- (b) KDB shall not normally make equity investments in any single enterprise in excess of either:
- (i) fifteen percent (15%) of the total unimpaired paid-up capital, surplus, and free reserves of KDB; or
  - (ii) fifty percent (50%) of the paid-up capital of the enterprise.
- (c) KDB shall not normally extend financial assistance (loan, investments and guarantees) to any single enterprise which exceed either of the following ceilings:
- (i) twenty-five percent (25%) of KDB's total unimpaired paid-up capital, surplus and free reserves;

- (ii) sixty-five percent (65%) of the total assets of the enterprise.

#### Foreign Exchange Risk

7. As a general policy, KDB shall cover itself adequately against foreign exchange risks in the conduct of its operations. However, in using "revolving funds" generated in the case of some foreign borrowings, KDB may assume the exchange risk temporarily. Also in using some funds provided under the Industrial Rationalization Fund Scheme, KDB may be exposed to the exchange risk. To cover the risk in the latter case, KDB will make provision amounting to 1.5% of such funds outstanding from time to time. Exchange losses exceeding the provision made by KDB, will be reimbursed by the Government.

#### Security Arrangements

- 8. (a) In accordance with normal business practices, KDB will obtain adequate security for its loans and guarantees. In extending a loan to an enterprise, KDB shall require such enterprise to provide security the value of which shall be not less than 125% of the amount of the loan. In the case of guarantees covered by a Government counter-guarantee the value of security shall be not less than the amount guaranteed, and in all other cases of guarantees, shall be not less than 120% of the principal amount covered under such guarantees.
- (b) KDB may waive any of the foregoing requirements in cases where the credit or the guarantee is extended in favor of those enterprises enumerated in para. 2, Article 10 of the Operating Manuals of KDB as of the date of this Policy Statement, provided, however, that in such cases KDB will endeavor to secure a guarantee or counter-guarantee from the Government or from a suitable bank or banks to cover the credit or guarantee granted.

#### Technical Assistance

9. KDB will endeavor to provide its subborrowers with the necessary technical services including assistance for upgrading production efficiency and solving complicated technical difficulties. It will observe the operation of its subborrowers and will, whenever necessary, promptly make available to them constructive and remedial advice on the operation of the project. When considered necessary, KDB will also dispatch its own staff to the project companies.

Management and Organization

10. To build and strengthen its own management and staff as well as to assist clients in the formulation and execution of their projects, KDB will maintain an effective organization and an adequate staff, including financial and economic analysis, engineering, accountancy, marketing and legal services.

Share-Holding Fund

11. KDB shall administer the Share-holding Administration Fund (the Fund) pursuant to the provisions of the KDB Share-holding Act (Act No. 2128, enacted August 4, 1969) as a separate and distinct account in KDB's official books, the Fund will be treated as segregated from the other transactions and resources of KDB in accordance with the provisions of said Act.

Financial Policies

12. KDB shall conduct its operations according to the provisions of the KDB Act. It shall endeavor to match the maturity of its liabilities with those of its assets. It will continually review the charges it levies for the financial assistance it provides to ensure that it receives an adequate "spread" to cover all its expenses including provisions for doubtful loans and investments, and to enable it to build reserves as required legally and as considered necessary by the management.

AEP Projects Department

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THE KOREA DEVELOPMENT BANK

Outline of Development Strategy for 1980-82

1. To achieve the goal of realizing an industrialized society, the Government will continue an export-oriented development strategy and an emphasis will be given to heavy and chemical industries on a selective basis through 1980s. As an instrument of the Government's development policy, KDB will in the three-year period 1980/82 further its development activities particularly in the specific areas outlined below.

2. Project Promotion and Resource Allocation

- (a) KDB will give priority financing to less energy-consuming, export-oriented industrial sectors such as machinery and electronics;
- (b) KDB will increase its emphasis on financing private sector projects;
- (c) KDB will expand its consultancy role to enterprises in the areas of project formulation, project design, selection of technology, engineering and project analysis;
- (d) KDB will continue to expand its contribution to the financial and industrial sectors through further development of its subsidiary companies - like KILC, SMBC, KASI and network of foreign offices;
- (e) KDB will endeavor to internationalize its banking operation by:
  - (i) establishment of new merchant bank abroad;
  - (ii) arrangement for inducement of foreign capital by private enterprises;
  - (iii) collateral administration for foreign lenders of non-guaranteed commercial loans; and
  - (iv) active operation of foreign exchange.
- (f) KDB will enhance its resource allocation efficiency by:
  - (i) giving priority to less energy-consuming projects in consideration of continued energy crisis;

- (ii) taking into account Korea's areas of international competitive advantage when evaluating export-oriented and import substitution projects;
- (iii) evaluating the forward and backward linkages of all capital and technology intensive projects; and
- (iv) scrutinizing carefully the employment impact of all industrial projects (with particular regard to regional distribution of employment and to income distribution effects) especially in consideration of recent economic slowdown.

3. Resource Mobilization. In line with its objective of intensifying its efforts at raising private resources, KDB plans to:

- (a) issue domestic bonds (IFDs) for a total amount of W 750 billion; and
- (b) borrow from the foreign commercial markets a total amount of US\$2.1 billion during the three-year period 1980-82.

4. Research and Inputs into Government Policy Formation. KDB plans to research the following items for the improvement of its operation and for the establishment of the Government policy:

- (a) industrial financing policy;
- (b) strategic industry in 1980s;
- (c) industrial financing system under open economy system;
- (d) strengthening of economic cooperation with foreign countries.

5. Organization

- (a) KDB will continue to enhance professional abilities of its staff through adequate training courses provided by domestic and foreign institutions;
- (b) to deal with the problem of data collection and processing, KDB will further develop computerization of its banking operations.

AEP Projects Department  
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Share of KDB's Disbursements in Fixed Investment, 1977-79  
(Won billion: current prices)

	Gross fixed capital formation 1977-79	KDB dis- bursements 1977-79	Share of KDB disbursements (%)
Agriculture, forestry & fishing	1.610	15	0.9
Mining and quarrying	142	21	14.9
Electricity, gas and water	2,067	359	17.4
Manufacturing	4,712	1,179	25.0
Construction	260	64	24.6
Wholesale & retail trade, restaurants & hotels	1,891	70	3.7
Transport, storage & communication	4,538	305	6.7
Financing, insurance, real estate & business services	159	22	13.8
Ownership of dwelling	3,605	-	-
Public administration	617	-	-
Community, social & personal services	1,185	-	-
<u>Total Fixed Capital Formation</u>	<u>20,788</u>	<u>2,038</u>	<u>9.8</u>



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Economic Impact of KDB Financed Projects, 1976-79  
Partial Economic Indicators of Projects /a  
(Won billion)

	1976	1977	1978	1979
No. of projects /b	587	679	789	698
Total project costs /c	434	697	1,140	1,431
Amount of KDB financing /c	226	345	579	940
Share of KDB financing (%)	52.1	49.5	50.8	65.7
Incremental annual sales /d	787	1,543	2,165	2,532
Incremental annual value Added /d	138	189	387	461
Increase in fixed assets	n.a.	n.a.	977	1,246
Additional employment ('000)	54	71	94	103
Additional annual payroll /d	25.2	33.4	45.0	50.1
Incremental annual exports /d	619	1,329	2,416	2,635
Net annual balance of payments effect (net foreign exchange earnings and savings) (\$ million) /d	n.a.	5,387	6,584	9,894
<u>Memorandum Items</u>				
Sales per additional employee (won '000)	14,574	21,732	23,032	24,582
Value added per additional employee (won '000)	2,556	2,662	4,117	4,476
Fixed assets per additional employee (won '000)	n.a.	n.a.	10,394	12,093
Annual payroll per additional employee (won '000)	466	471	479	486
Ratio of sales to fixed assets	n.a.	n.a.	2.2	2.0
Ratio of value added to fixed assets	n.a.	n.a.	0.4	0.37
Ratio of value added to sales	0.18	0.12	0.18	0.18
Export share of sales (%)	38	42	54	50
Payroll share of value added (%)	18	17	12	11

/a Based on projections made in project appraisal reports; equity investment and debenture financing are excluded.

/b Net of projects subsequently withdrawn.

/c Won equivalent at varying exchange rates.

/d Estimates at full capacity operations.

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Professional/a Staffing Position

As of December 31,	1976	1977	1978	1979
<b>A. Head Office</b>	<b>468</b>	<b>476</b>	<b>470</b>	<b>477</b>
1. <u>Support Departments</u>	<u>135</u>	<u>125</u>	<u>129</u>	<u>142</u>
Technical services	40	32	29	29
Business analysis & consultation	18	20	19	19
Research	41	38	36	36
Foreign capital	17	20	21	22
International	19	20	10	11
Management services				
2. <u>Operation Departments</u>	<u>156</u>	<u>163</u>	<u>150</u>	<u>122</u>
Loan department I	24	24	26	18
Loan department II	14	16	16	16
Foreign loan	19	17	19	18
Foreign guarantee	22	18	16	16
Share holding /b	28	40	32	-
Special loan /b	49	48	41	-
Loan administration /b	-	-	-	29
Special loan administration /b	-	-	-	25
3. <u>Planning &amp; Control Departments</u>	<u>93</u>	<u>106</u>	<u>93</u>	<u>110</u>
Planning	13	9	8	10
Business control	13	14	14	19
Finance Bond	18	23	13	27
Investment	8	14	17	16
Audit	22	25	19	18
EDPS /c	14	16	17	15
Management Improvement	5	5	5	5
4. <u>Administration Departments</u>	<u>63</u>	<u>55</u>	<u>72</u>	<u>75</u>
Personnel	30	26	37	39
General services	21	21	22	23
Security control	12	11	13	13
5. Others	21	24	26	28
<b>B. Branches</b>	<b>80</b>	<b>82</b>	<b>90</b>	<b>85</b>
Inchon Branch	6	7	8	7
Cheongju Branch	7	7	6	6
Daejeon Branch	8	8	8	9
Samcheog Branch	6	7	5	5
Jeonju Branch	5	6	6	6
Gwangju Branch	9	10	10	7
Daegu Branch	12	11	13	12
Busan Branch	21	19	19	18
Ulsan Branch	6	7	7	6
Changwon Branch	-	-	7	9
Temporary	-	-	1	-
<b>C. Representative Offices</b>	<b>11</b>	<b>15</b>	<b>20</b>	<b>22</b>
London	3	3	4	4
New York	4	4	5	4
Tokyo	3	3	4	4
Kuwait	1	1	1	1
Hong Kong	-	2	3	3
Singapore	-	2	3	3
Frankfurt	-	-	-	3
<u>Total Professionals</u>	<u>559</u>	<u>573</u>	<u>580</u>	<u>584</u>
<u>Total Staff</u>	<u>1,677</u>	<u>1,794</u>	<u>1,821</u>	<u>1,961</u>

/a KDB classifies all its staff at the Deputy Manager's level and above as professionals.

/b In 1979 Share Holding Dept. and Special Loan Dept. were integrated and divided into two: Loan Administration Dept. and Special Loan Administration Dept.

/c Previously EDPS & Accounting Dept.

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Summary of Loan Operations, 1976-79  
(Won million)

	1976 Amount	1977 Amount	1978 Amount	1979 No. /a	Amount
<u>Approvals</u>					
Domestic currency capital loans	147,738	245,873	406,350	277	545,624
Domestic currency working capital loans	47,472	58,929	59,878	222	204,684
<u>Total Domestic Currency Loans</u>	<u>195,210</u>	<u>304,802</u>	<u>466,228</u>	<u>499</u>	<u>750,308</u>
Foreign currency loans	34,498	41,582	121,845	204	207,495
<u>Total Approvals</u>	<u>229,708</u>	<u>346,384</u>	<u>588,073</u>	<u>703</u>	<u>957,803</u>
<u>Commitments</u>					
Domestic currency capital loans	147,121	245,873	406,350	277	545,624
Domestic currency working capital loans	47,345	58,929	59,878	222	204,684
<u>Total Domestic Currency Loans</u>	<u>194,466</u>	<u>304,802</u>	<u>466,228</u>	<u>499</u>	<u>750,308</u>
Foreign currency loans	34,066	41,403	121,845	199	205,385
<u>Total Commitments</u>	<u>228,532</u>	<u>346,205</u>	<u>588,073</u>	<u>698</u>	<u>955,693</u>
<u>Disbursements</u>					
Domestic currency capital loans	147,121	245,873	406,350	277	545,624
Domestic currency working capital loans	43,345	58,929	59,878	222	204,684
<u>Total Domestic Currency Loans /b</u>	<u>194,466</u>	<u>304,802</u>	<u>466,228</u>	<u>499</u>	<u>750,308</u>
Foreign currency loans /c	31,522	40,352	113,074	189	189,342
<u>Total Disbursements</u>	<u>225,988</u>	<u>345,154</u>	<u>579,302</u>	<u>688</u>	<u>939,650</u>
<u>Repayments</u>					
Domestic currency capital loans	23,634	40,307	77,501	42	93,047
Domestic currency working capital loans	34,376	27,217	51,965	71	82,014
<u>Total Domestic Currency Loans</u>	<u>58,010</u>	<u>67,524</u>	<u>129,466</u>	<u>113</u>	<u>175,061</u>
Foreign currency loans /c	5,905	9,624	14,260	49	70,027
<u>Total Repayments</u>	<u>63,915</u>	<u>77,148</u>	<u>143,726</u>	<u>162</u>	<u>245,088</u>
<u>Outstanding</u>					
Domestic currency capital loans	589,890	795,395	1,124,244	630	1,576,821
Domestic currency working capital loans	75,403	107,176	115,089	282	237,759
<u>Total Domestic Currency Loans</u>	<u>665,293</u>	<u>902,571</u>	<u>1,239,333</u>	<u>912</u>	<u>1,814,580</u>
Foreign currency loans	74,600	105,328	204,142	317	323,457
<u>Total Outstanding</u>	<u>739,893</u>	<u>1,007,899</u>	<u>1,443,475</u>	<u>1,229</u>	<u>2,138,037</u>

/a Number of loans (not available for 1976-78).

/b According to the standard banking practice in Korea, KDB credits its subborrowers' domestic currency loan accounts immediately after making a commitment. Consequently domestic currency commitments are equal to disbursements in all the years. The amounts not drawn down by the sub-borrowers from their respective loan accounts are shown under "Credit Control Account" - a current liability item.

/c Includes adjustments in loan amounts on account of exchange rate fluctuations.

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Characteristics of Loans Committed during 1977-79 and Outstanding as of December 31, 1979  
(Won million)

	Commitments						Outstanding as of December 31, 1979									
	1977		1978		1979		Capital loans			Working capital loans			Total			
	Amount	%	Amount	%	No./a	Amount	%	No./b	Amount	%	No./b	Amount	%	No./a	Amount	%
<b>Type of Assistance</b>																
Domestic currency	304,802	88.0	466,228	79.3	499	750,308	78.5	388	1,576,821	83.0	146	237,759	100.0	912	1,814,580	84.9
Foreign currency	41,403	12.0	121,845	20.7	199	205,385	21.5	173	323,457	17.0	-	-	-	317	323,457	15.1
<b>Total</b>	<b>346,205</b>	<b>100.0</b>	<b>588,073</b>	<b>100.0</b>	<b>698</b>	<b>955,693</b>	<b>100.0</b>	<b>561</b>	<b>1,900,278</b>	<b>100.0</b>	<b>146</b>	<b>237,759</b>	<b>100.0</b>	<b>1,229</b>	<b>2,138,037</b>	<b>100.0</b>
<b>Ownership</b>																
Private sector	211,162	61.0	290,688	49.4	625	526,778	55.1	499	906,433	47.7	143	211,606	89.0	1,119	1,118,039	52.3
Public sector	135,043	39.0	297,385	50.6	73	428,915	44.9	62	993,845	52.3	3	26,153	11.0	110	1,019,998	47.7
Of which companies under SAF	-	-	(6,824)	(1.2)	(2)	(81,234)	(8.5)	(1)	(78,780)	(4.1)	(1)	(4,100)	(1.7)	(5)	(82,880)	(3.9)
<b>Total</b>	<b>346,205</b>	<b>100.0</b>	<b>588,073</b>	<b>100.0</b>	<b>698</b>	<b>955,693</b>	<b>100.0</b>	<b>561</b>	<b>1,900,278</b>	<b>100.0</b>	<b>146</b>	<b>237,759</b>	<b>100.0</b>	<b>1,229</b>	<b>2,138,037</b>	<b>100.0</b>
<b>Nature of Project</b>																
New	98,286	28.4	199,357	33.9	156	257,464	26.9	168	729,361	38.4	-	-	-	303	729,361	34.1
Expansion	182,130	52.6	325,898	55.4	246	464,180	48.6	359	1,140,446	60.0	-	-	-	496	140,446	53.4
BMR /c	6,860	2.0	2,940	0.5	75	25,899	2.7	34	30,471	1.6	-	-	-	148	30,471	1.4
Working capital	58,929	17.0	39,878	10.2	221	208,150	21.8	-	-	-	146	237,759	100.0	282	237,759	11.1
<b>Total</b>	<b>346,205</b>	<b>100.0</b>	<b>588,073</b>	<b>100.0</b>	<b>698</b>	<b>955,693</b>	<b>100.0</b>	<b>561</b>	<b>1,900,278</b>	<b>100.0</b>	<b>146</b>	<b>237,759</b>	<b>100.0</b>	<b>1,229</b>	<b>2,138,037</b>	<b>100.0</b>
<b>Size of Loan (W million)</b>																
Up to 50	7,526	2.2	6,944	1.2	75	11,045	1.1	153	30,181	1.6	n.a.	4,582	1.9	183	34,763	1.6
50-100	20,127	5.8	21,640	3.6	186	40,084	4.2	102	53,257	2.8	n.a.	12,419	5.1	246	65,676	3.1
100-300	46,474	13.4	51,043	8.7	122	129,993	13.6	96	175,692	9.2	n.a.	20,863	8.8	295	196,555	9.2
300-1,000	106,018	30.6	125,698	21.4	172	263,698	27.6	114	439,170	23.1	n.a.	62,185	26.2	241	501,355	23.4
1,000-2,000	50,311	14.5	96,945	16.5	125	197,694	20.7	54	299,184	15.8	n.a.	49,201	20.7	232	348,385	16.3
Over 2,000	115,749	33.5	285,803	4.8	18	313,179	32.8	42	902,794	47.5	n.a.	88,509	3.7	32	991,303	46.4
<b>Total</b>	<b>346,205</b>	<b>100.0</b>	<b>588,073</b>	<b>100.0</b>	<b>698</b>	<b>955,693</b>	<b>100.0</b>	<b>561</b>	<b>1,900,278</b>	<b>100.0</b>	<b>n.a.</b>	<b>237,759</b>	<b>100.0</b>	<b>1,229</b>	<b>2,138,037</b>	<b>100.0</b>
<b>Maturities</b>																
<b>Capital Loans</b>																
Up to 4 years	1,276	0.3	2,531	0.5	22	2,748	0.3	23	3,521	0.2	-	-	-	26	3,521	0.2
4-8 years	165,615	57.7	251,530	47.6	199	410,029	54.9	212	990,273	52.1	-	-	-	391	990,273	52.1
8-10 years	49,558	17.3	190,150	36.0	102	233,075	31.2	124	436,230	23.0	-	-	-	262	436,230	23.0
10-15 years	23,594	8.2	60,742	11.5	54	71,687	9.6	96	141,039	7.4	-	-	-	119	141,039	7.4
Over 15 years	47,236	16.5	23,242	4.4	76	29,975	4.0	106	329,215	17.3	-	-	-	173	329,215	17.3
<b>Subtotal</b>	<b>287,279</b>	<b>100.0</b>	<b>528,195</b>	<b>100.0</b>	<b>453</b>	<b>747,514</b>	<b>100.0</b>	<b>561</b>	<b>1,900,278</b>	<b>100.0</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>971</b>	<b>1,900,278</b>	<b>100.0</b>
<b>Working Capital Loans</b>																
Up to 6 months	1,424	2.4	5,629	9.4	110	47,007	22.6	-	-	-	38	32,782	13.8	42	32,782	13.8
1/2-1 year	23,942	40.6	18,981	31.7	42	58,019	27.9	-	-	-	25	62,912	26.5	67	62,912	26.5
1-2 years	9,029	15.3	9,700	16.2	31	26,918	12.9	-	-	-	29	43,087	18.1	52	43,087	18.1
2-3 years	20,169	34.3	19,640	32.8	49	50,004	24.0	-	-	-	37	67,941	28.6	73	67,941	28.6
Over 3 years	4,365	7.4	5,928	9.9	13	26,231	12.6	-	-	-	17	31,037	13.0	24	31,037	13.0
<b>Subtotal</b>	<b>58,929</b>	<b>100.0</b>	<b>59,878</b>	<b>100.0</b>	<b>245</b>	<b>208,179</b>	<b>100.0</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>146</b>	<b>237,759</b>	<b>100.0</b>	<b>258</b>	<b>237,579</b>	<b>100.0</b>
<b>Total</b>	<b>346,205</b>	<b>-</b>	<b>588,073</b>	<b>-</b>	<b>698</b>	<b>955,693</b>	<b>-</b>	<b>-</b>	<b>1,900,278</b>	<b>-</b>	<b>-</b>	<b>237,759</b>	<b>-</b>	<b>1,229</b>	<b>2,138,037</b>	<b>-</b>

/a Number of loans (not available for some years and categories).

/b Number of companies (not available for some categories).

/c Balancing, modernization and replacement.

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Sectoral and Geographical Distribution of Loans Committed during 1977-79 and Outstanding as of December 31, 1979  
(Won million)

	Commitments						Outstanding as of December 31, 1979										
	1977		1978		1979		Capital loan			Operating loans			Total		No./a	Amount	%
	Amount	%	Amount	%	No./a	Amount	%	No./b	Amount	%	No./b	Amount	%				
<b>Sectoral Distribution</b>																	
<u>Manufacturing Industries</u>	<u>208,157</u>	<u>60.1</u>	<u>289,605</u>	<u>49.2</u>	<u>414</u>	<u>548,614</u>	<u>57.4</u>	<u>349</u>	<u>853,978</u>	<u>44.9</u>	<u>123</u>	<u>209,678</u>	<u>88.2</u>	<u>738</u>	<u>1,063,656</u>	<u>49.8</u>	
<u>Consumer Goods</u>	<u>16,324</u>	<u>4.7</u>	<u>14,622</u>	<u>2.5</u>	<u>62</u>	<u>51,799</u>	<u>5.4</u>	<u>73</u>	<u>60,291</u>	<u>3.2</u>	<u>31</u>	<u>28,837</u>	<u>12.1</u>	<u>143</u>	<u>89,128</u>	<u>4.2</u>	
Of which:																	
Textiles, wearing apparel & leather	13,837	4.0	11,363	1.9	41	32,207	3.4	41	42,032	2.2	24	25,939	10.9	102	67,971	3.2	
<u>Intermediate Goods</u>	<u>68,968</u>	<u>19.9</u>	<u>101,158</u>	<u>17.2</u>	<u>133</u>	<u>171,929</u>	<u>18.0</u>	<u>134</u>	<u>293,386</u>	<u>15.4</u>	<u>44</u>	<u>61,963</u>	<u>26.1</u>	<u>212</u>	<u>355,349</u>	<u>16.6</u>	
Of which:																	
Chemicals, rubber & plastics	45,789	13.2	44,871	7.6	52	39,470	4.1	50	115,026	6.0	19	22,027	9.3	82	137,053	6.4	
Petroleum & coal	3,282	1.0	4,874	0.8	12	50,461	5.3	11	58,548	3.1	4	4,744	2.0	11	63,292	3.0	
<u>Capital Goods</u>	<u>122,488</u>	<u>35.4</u>	<u>173,584</u>	<u>29.5</u>	<u>212</u>	<u>322,642</u>	<u>33.8</u>	<u>125</u>	<u>499,083</u>	<u>26.2</u>	<u>45</u>	<u>118,645</u>	<u>49.9</u>	<u>370</u>	<u>617,728</u>	<u>28.9</u>	
Of which:																	
Metals	50,680	14.7	114,496	18.4	120	177,377	18.6	70	325,910	17.1	22	52,648	22.1	177	378,558	17.7	
Machinery	38,787	11.2	26,667	4.6	45	65,943	6.9	38	70,038	3.7	14	35,849	15.1	68	105,887	5.0	
Others	377	0.1	241	0.0	7	2,244	0.2	17	1,218	0.1	3	233	0.1	13	1,451	0.1	
<u>Nonmanufacturing Industries</u>	<u>138,048</u>	<u>39.9</u>	<u>298,468</u>	<u>50.8</u>	<u>284</u>	<u>407,079</u>	<u>42.6</u>	<u>212</u>	<u>1,046,300</u>	<u>55.1</u>	<u>23</u>	<u>28,081</u>	<u>11.8</u>	<u>491</u>	<u>1,074,381</u>	<u>50.2</u>	
Of which:																	
Elec. & waterworks	56,363	16.3	148,458	25.5	73	154,400	16.2	27	540,001	28.4	2	1,084	0.5	96	541,085	25.3	
Transportation	41,775	12.2	82,430	14.0	121	169,253	17.7	74	349,495	18.4	9	9,448	4.0	223	358,943	16.8	
<u>Total</u>	<u>346,205</u>	<u>100.0</u>	<u>588,073</u>	<u>100.0</u>	<u>698</u>	<u>955,693</u>	<u>100.0</u>	<u>561</u>	<u>1,900,278</u>	<u>100.0</u>	<u>146</u>	<u>237,759</u>	<u>100.0</u>	<u>1,229</u>	<u>2,138,037</u>	<u>100.0</u>	
<b>Geographical Distribution</b>																	
Seoul City	141,332	40.8	251,107	42.7	285	394,415	41.3	207	886,340	46.7	46	97,585	41.0	440	983,925	46.0	
Busan City	27,131	7.9	28,228	4.8	29	77,507	8.1	58	138,736	7.3	11	15,630	6.6	121	154,366	7.2	
Gyeonggi Province	49,405	14.3	56,455	9.6	82	90,886	9.5	93	207,211	10.9	26	25,407	10.7	124	232,618	10.9	
South Chung-Cheong Province	640	0.2	5,881	1.0	19	21,216	2.2	11	28,390	1.5	5	1,778	0.8	29	30,168	1.4	
North Chung-Cheong Province	4,656	1.3	13,526	2.3	35	41,668	4.4	9	36,757	1.9	6	2,996	1.3	43	39,753	1.9	
Kang-Won Province	11,875	3.4	9,999	1.7	37	30,678	3.2	21	38,861	2.0	4	5,781	2.4	69	44,642	2.1	
South Jeon-ra Province	28,850	8.3	57,041	9.7	71	67,759	7.1	22	161,248	8.5	11	22,837	9.6	102	184,085	8.6	
North Jeon-ra Province	2,745	0.8	2,352	0.4	25	25,140	2.6	6	17,280	1.0	1	6,025	2.5	43	23,305	1.1	
South Kyung-Sang Province	55,562	16.1	98,796	16.8	56	119,366	12.5	78	251,160	13.2	16	31,916	13.4	145	283,076	13.2	
North Kyung-Sang Province	24,009	6.9	64,688	11.0	42	82,183	8.6	49	129,613	6.8	19	27,747	11.7	82	157,360	7.4	
Che-ju Island	-	-	-	-	17	4,875	0.5	7	4,682	0.2	1	57	0.0	31	4,739	0.2	
<u>Total</u>	<u>346,205</u>	<u>100.0</u>	<u>588,073</u>	<u>100.0</u>	<u>698</u>	<u>955,693</u>	<u>100.0</u>	<u>561</u>	<u>1,900,278</u>	<u>100.0</u>	<u>146</u>	<u>237,759</u>	<u>100.0</u>	<u>1,229</u>	<u>2,138,037</u>	<u>100.0</u>	

/a Number of loans (not available for 1977-78).

/b Number of companies.

AEP Projects Dept.  
March 15, 1980

## KOREA

## THE KOREA DEVELOPMENT BANK

Subprojects Approved Under Bank Loan No. 1338-KO  
(US\$'000)

Sub-borrower	Industry	Type of project	Total project cost		KDB financing		Rate of return (%)		Incremental annual exports	Incremental employment (number)	Cost per job
			Local	Foreign	Total	IBRD	Financial	Economic			
Korea Bearing Industry Co., Ltd.	Machinery	Expansion	7,863	4,997	4,997	4,997	30.0	41.7	-	279	34
Sudo Industrial Co., Ltd.	Textile	Expansion	258	377	377	377	-	-	3,100	176	3
Cho Sun Silk Textile Co., Ltd.	Textile	Expansion	1,474	923	923	923	23.4	46.2	1,277	150	11
Doo San Manufacturing Co., Ltd.	Machinery	Expansion	2,050	1,104	1,117	395	-	-	-	174	14
Dae Woo Heavy Industry, Ltd.	Machinery	Expansion	7,409	4,996	6,146	4,996	21.2	30.4	4,443	471	17
Bookook Steel & Wire Co., Ltd.	Metal	Expansion	1,544	1,924	1,718	1,718	21.5	22.5	3,616	60	49
Tong Myung Heavy Industries Co., Ltd.	Machinery	Expansion	4,749	4,299	5,179	4,009	25.6	34.1	-	289	24
Sam Sung Radiator Industry Co., Ltd.	Machinery	Expansion	1,476	632	632	632	-	-	-	215	9
Sam Hwa Trading Co.	Paper	Expansion	252	804	804	804	25.3	25.8	-	63	17
Pacific Development Co., Ltd.	Glass	Expansion	683	733	733	733	-	-	1,080	54	26
Sam Hwa Printing Co., Ltd.	Printing	Expansion	252	406	406	406	-	-	176	8	82
Hyun Dai Cement Co., Ltd.	Cement	Expansion	627	855	855	855	19.2	24.9	1,050	20	74
Man Jeong Industrial Co., Ltd.	Mining	Expansion	2,600	2,050	2,654	2,050	19.0	29.6	-	108	43
Sung Shin Cement Ind. Co., Ltd.	Cement	Expansion	537	1,211	1,211	1,211	-	-	-	-	-
Mijin Metal Ind. Co., Ltd.	Metal	Expansion	2,617	3,946	3,946	3,946	19.2	25.8	6,807	820	8
Dong Ah Construction Co., Ltd.	Construction	Expansion	38,907	1,800	1,800	1,800	17.7	22.8	1,755	274	149
Yu Han Corporation	Pharmaceutical	Expansion	3,997	486	367	367	-	-	-	-	-
Korea Synthetic Rubber Ind. Co., Ltd.	Rubber	Expansion	3,450	2,759	3,060	2,689	16.6	20.6	9,783	56	86
Kumho Tire & Rubber Inc.	Rubber	Expansion	11,392	5,614	5,309	5,000	15.0	31.5	39,904	529	32
Shin Young Co., Ltd.	Textile	Expansion	173	558	558	558	-	-	-	45	16
Chunilsa Elec. Ind. Co., Ltd.	Machinery	Expansion	2,654	1,006	743	743	-	-	23,352	90	1
Dong Yang Machinery Co., Ltd.	Machinery	Expansion	8,604	5,000	5,000	5,000	35.1	36.7	-	1,157	12
Shinhan Shipping Co., Ltd.	Shipping	Expansion	2,344	1,142	1,142	1,142	12.3	12.5	-	28	125
Pacific Metals Co., Ltd.	Mining	New	2,942	1,954	1,954	1,954	23.5	32.9	-	179	27
Tong Yang Express Ferry Co., Ltd.	Shipping	Expansion	154	5,308	5,000	5,000	21.2	15.3	-	86	64
Pyung Hwa Dang Printing Co., Ltd.	Printing	Expansion	237	289	289	289	-	-	-	14	27
Kong Yung Sa Co., Ltd.	Mineral	Expansion	1,013	529	529	529	-	-	-	-	-
Kumpoong Industrial Co., Ltd.	Paper	Expansion	655	730	730	730	-	-	477	53	23
Korea Zinc Co., Ltd.	Metal	New	42,635	25,000	5,361	4,000	21.7	24.5	14,791	495	137
Choyang Shipping Co., Ltd.	Shipping	Expansion	15,065	7,640	15,260	5,000	16.1	16.5	5,910	80	284
Han Jin Shipping Co., Ltd.	Shipping	Expansion	1,304	483	1,493	483	-	-	1,906	24	74
Hyundai Precision and Industry Co., Ltd.	Transportation	New	767	720	720	720	-	-	19,421	122	12
Seo Han Development Co., Ltd.	Metal	Expansion	1,520	326	326	326	-	-	3,775	55	34
Iljin Metal Manufacturing Company	Metal	New	641	950	950	950	24.0	33.8	3,600	68	23
Ssang Yong Shipping Co., Ltd.	Shipping	Expansion	1,798	6,150	500	5,000	18.5	27.1	-	27	294
Han Kuk Dropforging Co., Ltd.	Metal	Expansion	3,142	5,743	6,252	1,787	25.9	37.5	-	173	51
Heung-A Shipping Co., Ltd.	Shipping	Expansion	3,510	1,155	3,184	1,132	21.7	24.4	3,425	46	101

## KOREA

## THE KOREA DEVELOPMENT BANK

Subprojects Approved Under Bank Loan No. 1574-KO  
(US\$'000)

Subborrower	Industry	Type of project	Total project cost		KDB financing		Maturity	Rate of return (%)		Incremental annual exports	Incremental employment (number)	Cost per job
			Local	Foreign	Total	IBRD		Financial	Economic			
Dong Yang Tinplate Ind. Co., Ltd.	Metal	Exp	1,933	794	794	794	10	17.6	36.1	-	-	-
Pyeong Hwa Clutch Co., Ltd.	Metal	Exp	1,597	300	300	300	6	-	-	-	46	41
Hyundai Rolling Stock Co., Ltd.	Machinery	New	22,108	6,802	8,072	5,006	12.5	26.2	33.9	57,938	1,505	19
Tong Myung Development Co., Ltd.	Construction	Exp	2,442	998	998	998	6	11.7	14.3	-	72	48
Yuseung Metal Industrial Co., Ltd.	Metal	New	823	300	300	300	10	-	-	198	29	39
Han Jin Transportation Co., Ltd.	Transportation	Exp	12,147	4,660	4,660	4,660	11	25.5	47.9	-	217	77
Poong Man Paper Mfg. Co., Ltd.	Paper	Exp	19,965	7,500	9,562	7,500	12.5	20.5	17.1	-	512	54
Dae Rim Pulp Co., Ltd.	Paper	New	10,282	4,659	6,308	4,659	12	19.0	30.2	-	252	59
Dae Rim Pulp Co., Ltd.	Paper	Exp	2,601	1,720	2,132	1,720	12	24.8	30.5	-	79	55
Sam Kyung Chemical Co., Ltd.	Chemical	Exp	3,922	4,572	4,572	4,572	12	37.3	12.4	-	47	181
Holy Paper Mfg. Co., Ltd.	Paper	Exp	820	687	687	687	9	-	-	3,485	24	63
Sam Sung Special Paper Mfg. Co., Ltd.	Paper	Exp	5,215	2,000	2,000	2,000	12	35.4	24.4	-	174	41
Pyung Hwa Dang Printing Co., Ltd.	Printing	Exp	508	737	737	737	10	14.0	23.3	-	10	125
Ssang Yong Shipping Co., Ltd.	Transportation	Exp	8,526	2,715	3,509	2,415	15	10.0	10.7	1,180	31	363
Samhwa Electric Co., Ltd.	Machinery	Exp	3,512	1,870	1,870	1,870	10	19.5	33.5	3,736	35	154
Taikwang Metallic Card Cloth Co., Ltd.	Machinery	New	945	640	640	640	10	-	-	-	54	30
Samsung Electronics Co., Ltd.	Machinery	New	20,010	5,019	5,019	5,019	10	14.1	46.9	121,954	342	73
Han Kuk Drop Forging Co., Ltd.	Machinery	Exp	4,198	7,159	7,658	2,999	12	23.9	33.4	-	176	65
Tae Sung Mechanical Industries Co., Ltd.	Construction	Exp	437	675	819	675	6	-	-	-	9	124
Hanjin Container Lines Ltd.	Transportation	Exp	26,191	11,500	26,680	7,500	12	29.2	30.4	39,241	218	173
Mi Ryung Construction Co., Ltd.	Construction	Exp	13,024	320	960	960	6	11.5	13.4	-	18	741
Sanjin Aluminium Co., Ltd.	Paper	Exp	968	587	587	587	8	-	-	-	20	78
Kyung Nam Sumyu Ind. Co., Ltd.	Textile	Exp	1,036	762	762	762	10	24.1	39.2	1,994	12	150
Ssang Young Spinning Co., Ltd.	Textile	Exp	9,243	9,068	7,526	5,150	11	22.7	49.7	18,747	357	51
K-Mek Inc.	Metal	Exp	1,385	895	895	895	10	27.0	34.3	3,432	32	71
Nam Sun Machinery Works	Machinery	Exp	228	610	610	610	10	19.6	26.5	1,083	93	9
Bo Sung Special Fiber Co., Ltd.	Textile	Exp	773	892	892	892	11	28.6	41.8	1,539	28	59
Union Co., Ltd.	Chemical	Exp	7,592	5,267	4,950	4,950	14	21.0	27.6	1,992	44	292
Chun Kwang Ceramic Ltd.	Mineral	New	1,569	980	980	980	10	21.4	28.8	2,111	303	8
Apollo Ltd.	Mineral	Exp	2,068	999	994	994	12	21.5	37.6	5,553	75	41
Chun Kyung Container Terminal Co., Ltd.	Transportation	Exp	408	519	519	519	8	21.2	31.3	336	17	54
Dong Yang Steel Ind. Co., Ltd.	Metal	Exp	4,794	6,467	7,352	6,467	10	18.8	25.8	7,570	43	262
Dong Bu Travel Service Co., Ltd.	Transportation	Exp	3,294	2,241	2,241	2,241	10	16.4	28.6	-	162	34
Han Bo General Construction Co., Ltd.	Construction	Exp	1,684	380	380	380	5	-	-	-	132	16
Yoonshin Industry Co., Ltd.	Metal	New	791	1,301	1,301	1,301	10	32.5	45.5	-	42	50
Kuk Je Pharma. Ind. Co., Ltd.	Chemical	Exp	946	378	587	587	9	-	-	-	20	66
Korea Steel Chemical Co., Ltd.	Chemical	New	7,068	4,000	4,000	4,000	10	16.6	18.4	6,365	100	111
Media Corporation	Chemical	Exp	1,686	961	961	961	7	18.1	33.2	4,976	63	42
Han Jun Petro-Chemical Mfg. Co., Ltd.	Chemical	New	3,728	716	716	716	8	-	-	-	3	931
Shin Young Co., Ltd.	Textile	Exp	473	1,781	1,781	1,781	9	16.4	19.7	3,795	230	24
Cheil Leather Co., Ltd.	Leather	Exp	198	343	343	343	9	-	-	2,406	20	41
Dae Won Worsted Spinning Co., Ltd.	Textile	Exp	198	573	573	573	9	-	-	2,565	100	8
Orient Watch Industrial Co., Ltd.	Machinery	Exp	4,237	2,224	400	400	7	-	-	3,445	896	7
<b>Total</b>			<b>217,453</b>	<b>107,571</b>							<b>6,642</b>	<b>48.9</b>

KOREA

THE KOREA DEVELOPMENT BANK

Summary of Investment Operations, 1976-79  
(Won million)

	1976	1977	1978	1979
<u>Equity Investment</u>				
Total investment at the beginning of the year	131,595	160,238	217,361	273,516
New Investments During the Year				
Direct purchases	38,619	61,551	77,714	24,495
Loan conversions	2,200	2,066	5,550	2,380
Transfer from Government	-	-	-	-
Subtotal	<u>40,819</u>	<u>63,617</u>	<u>83,264</u>	<u>26,875</u>
Investments sold during the year	12,176	6,494	27,109	-
<u>Net Investments at the End of the Year</u>				
Direct purchases	84,554	140,469	209,952	234,447
Loan conversions	20,336	22,294	9,796	12,176
Transfer from Government	55,348	54,598	53,768	53,768
Total at the End of the Year	<u>160,238</u>	<u>217,361</u>	<u>273,516</u>	<u>300,391</u>
<u>Bonds and Debentures</u>				
Total investment at the beginning of the year	13,524	17,527	23,236	26,384
New investments during the year	4,841	8,241	3,755	8,983
Investments sold during the year	838	2,532	607	3,576
Net investments at the end of the year	<u>17,527</u>	<u>23,236</u>	<u>26,384</u>	<u>31,791</u>
<u>Total Investments</u>				
Total investment at the beginning of the year	145,119	177,765	240,597	299,900
New investments during the year	45,660	71,858	87,019	35,858
Investments sold during the year	13,014	9,026	27,716	3,576
Net investments at the end of the year	<u>177,765</u>	<u>240,597</u>	<u>299,900</u>	<u>332,182</u>
<u>Income from Investment Portfolio</u>				
Dividend income	3,719	5,572	5,748	12,349
(as % of the average equity investments)	(2.5)	(3.0)	(2.3)	(4.3)
Capital gains realized	4,861	5,640	7,991	538/a
(as % of cost of investment sold)	(39.9)	(86.8)	(29.5)	-
Dividend income plus capital gains	8,580	11,212	13,739	12,887
(as % of average equity investments)	(5.9)	(5.9)	(5.6)	(4.5)
Interest income from bonds and debentures	1,254	1,807	2,408	2,821
(as % of average bond & debentures investments)	(8.1)	(8.9)	(9.7)	(9.7)
Total income from total investment portfolio	9,834	13,019	16,147	15,708
(as % of total average investment portfolio)	(6.1)	(6.2)	(6.0)	(5.0)

/a Capital gains realized from the sale of bonds and debentures.



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THE KOREA DEVELOPMENT BANK

Characteristics of Equity Investments Committed During 1977-79 and Outstanding as of December 31, 1979  
(Won million)

	Commitments during the year									Outstanding as of		
	1977			1978			1979			December 31, 1979		
	No. /a	Amount	%	No. /a	Amount	%	No. /a	Amount	%	No. /b	Amount	%
<u>Type of Investment</u>												
Domestic currency	35	62,323	98.0	26	82,416	99.0	16	25,834	96.1	34	298,625	99.4
Foreign currency	1	1,294	2.0	4	848	1.0	1	1,041	3.9	3	1,766	0.6
<u>Total</u>	<u>36</u>	<u>63,617</u>	<u>100.0</u>	<u>30</u>	<u>83,264</u>	<u>100.0</u>	<u>17</u>	<u>26,875</u>	<u>100.0</u>	<u>37</u>	<u>300,391</u>	<u>100.0</u>
<u>Ownership</u>												
Private sector	18	9,232	14.5	8	9,773	11.7	15	12,433	46.3	22	73,690	24.5
Public sector	18	54,385	85.5	22	73,491	88.3	2	14,442	53.7	15	226,701	75.5
(Of which companies under SAF)	(2)	(1,541)	(2.4)	(2)	(827)	(1.0)	(1)	(800)	(3.0)	(1)	(800)	(0.3)
<u>Total</u>	<u>36</u>	<u>63,617</u>	<u>100.0</u>	<u>30</u>	<u>83,264</u>	<u>100.0</u>	<u>17</u>	<u>26,875</u>	<u>100.0</u>	<u>37</u>	<u>300,391</u>	<u>100.0</u>
<u>Nature of Project</u>												
New	7	5,039	7.9	2	14,591	17.5	3	11,867	44.2	11	42,712	14.2
Existing	29	58,578	92.1	28	68,673	82.5	14	15,008	55.8	26	257,679	85.8
<u>Total</u>	<u>36</u>	<u>63,617</u>	<u>100.0</u>	<u>30</u>	<u>83,264</u>	<u>100.0</u>	<u>17</u>	<u>26,875</u>	<u>100.0</u>	<u>37</u>	<u>300,391</u>	<u>100.0</u>
<u>Size of Investment (W million)</u>												
Up to 50	9	263	0.4	5	187	0.2	1	13	/c	3	70	/c
50-100	6	524	0.8	3	229	0.3	1	97	0.4	1	89	/c
100-300	4	719	1.1	3	635	0.8	-	-	-	1	187	/c
300-1,000	8	4,992	7.9	7	4,657	5.6	4	2,193	8.2	10	4,886	1.6
1,000-2,000	5	6,123	9.6	5	6,166	7.4	-	-	-	6	9,745	3.3
Over 2,000	4	50,996	80.2	7	71,396	85.7	11	24,572	91.4	16	285,414	95.0
<u>Total</u>	<u>36</u>	<u>63,617</u>	<u>100.0</u>	<u>30</u>	<u>83,264</u>	<u>100.0</u>	<u>17</u>	<u>26,875</u>	<u>100.0</u>	<u>37</u>	<u>300,391</u>	<u>100.0</u>
<u>Sectoral Disbursement</u>												
Manufacturing Industries	13	58,213	91.5	21	69,950	84.0	10	20,130	74.9	11	222,565	74.1
Consumer goods	3	3,091	4.7	6	2,073	2.5	-	-	-	-	-	-
Intermediate goods	4	21,403	33.6	6	25,400	30.5	-	-	-	4	84,918	28.3
Capital goods	6	33,809	53.2	9	42,477	51.0	10	20,130	74.9	5	137,472	45.7
Other	-	-	-	-	-	-	-	-	-	2	175	0.1
Nonmanufacturing Industries	23	5,404	8.5	9	13,314	16.0	7	6,745	25.1	26	77,826	25.9
<u>Total</u>	<u>36</u>	<u>63,617</u>	<u>100.0</u>	<u>30</u>	<u>83,264</u>	<u>100.0</u>	<u>17</u>	<u>26,875</u>	<u>100.0</u>	<u>37</u>	<u>300,391</u>	<u>100.0</u>
<u>Geographical Distribution</u>												
Seoul City	15	24,053	37.8	9	31,054	37.3	6	8,905	33.1	22	128,761	42.9
Busan City	1	100	0.1	-	-	-	-	-	-	-	-	-
Kyunggi Province	-	-	-	-	-	-	-	-	-	3	14,261	4.7
South Chung-Cheong Province	1	103	0.2	-	-	-	-	-	-	1	14,042	4.7
North Chung-Cheong Province	2	3,936	14.0	7	13,850	16.6	-	-	-	-	-	-
Kang-Won Province	3	223	0.4	-	-	-	-	-	-	-	-	-
South Jeon-ra Province	-	-	-	-	-	-	-	-	-	-	-	-
North Jeon-ra Province	1	37	0.1	-	-	-	-	-	-	-	-	-
South Kyung-Sang Province	5	4,069	6.4	3	4,290	5.2	9	16,073	59.8	4	35,210	11.7
North Kyung-Sang Province	7	25,370	39.9	9	32,400	38.9	1	1,800	6.7	3	105,178	35.0
Che-ju Island	-	-	-	-	-	-	-	-	-	-	-	-
Other	1	726	1.1	2	1,670	2.0	1	97	0.4	4	2,939	1.0
<u>Total</u>	<u>36</u>	<u>63,617</u>	<u>100.0</u>	<u>30</u>	<u>83,264</u>	<u>100.0</u>	<u>17</u>	<u>26,875</u>	<u>100.0</u>	<u>37</u>	<u>300,391</u>	<u>100.0</u>

/a Number of investment operations.

/b Number of companies.

/c Less than 0.1%.

KOREA

THE KOREA DEVELOPMENT BANK

Summary of Guarantee Operations, 1977-79  
(Won million)

	<u>Commitments during the year</u>			<u>Outstanding as of December 31,</u>		
	1977	1978	1979	1977	1978	1979
<u>Foreign Currency</u>						
<u>Guarantees /a</u>	1,035,591	1,446,598	1,073,693	3,207,530	3,805,599	3,580,790
Of which:						
Covered under GRA /b	621,712	1,035,767	622,372	2,538,312	2,968,636	2,707,197
Covered by GOK /c	-	1,669	451	19,415	11,531	5,134
Of which:						
also covered						
under GRA	-	1,614	451	9,570	9,572	4,423
<u>Domestic currency</u>						
<u>guarantees</u>	60,761	40,675	68,750	71,314	92,739	141,420
<u>Total Guarantees</u>	<u>1,096,352</u>	<u>1,487,273</u>	<u>1,142,443</u>	<u>3,278,844</u>	<u>3,898,338</u>	<u>3,722,210</u>
Guarantees redeemed	329,200	867,779	1,318,571	-	-	-
Guarantee commission						
earned	-	-	-	12,999	15,972	17,087
(As % of average out-						
standing guarantees)	-	-	-	0.40	0.41	0.46

/a New foreign currency guarantees issued during the years 1977 through 1979 can be reconciled with Table 12 after the following adjustments:

	1977	1978	1979
New foreign currency guarantees	956,730	780,123	503,128
Increase from variations in foreign exchange rates	227,372	445,575	279,492
Other increases	(213,267)	27,694	55,168
Guarantees on letter of credit	5,330	193,206	235,904
<u>Total</u>	<u>1,035,591</u>	<u>1,446,598</u>	<u>1,073,692</u>

Increases from variations in foreign exchange rates arise because of KDB's policy to adjust the recorded value of foreign currency guarantees at the time a transaction occurs in respect of specific guarantees.

/b Guarantee Release Agreement dated March 31, 1975 between the Government of Korea and KDB.

/c Behest loans.

AEP Projects Department  
March 15, 1980

KOREA

THE KOREA DEVELOPMENT BANK

Characteristics of Guarantees Committed During 1977-79 and Outstanding as of December 31, 1979  
(Won million)

	Commitments during the year /a						Outstanding as of		
	1977		1978		1979		December 31, 1979/b		
	Amount	%	Amount	%	Amount	%	No. /c	Amount	%
<b>Type of Assistance</b>									
Domestic currency	60,761	6.0	40,675	5.0	68,750	12.0	63	141,420	3.8
Foreign currency	956,730	94.0	780,123	95.0	503,128	88.0	76	3,580,790	96.2
<b>Total</b>	<b>1,017,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>
<b>Ownership</b>									
Private sector	589,119	57.9	532,785	64.9	403,176	70.5	130	1,989,247	53.4
Public sector	428,372	42.1	288,013	35.1	168,702	29.5	9	1,732,963	46.6
(Of which companies under SAF)	(636)	(0.1)	(1,191)	(0.1)	(4,311)	(0.8)	(1)	(12,423)	(0.3)
<b>Total</b>	<b>1,017,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>
<b>Nature of Project</b>									
New	439,287	43.2	143,949	17.5	336,015	58.8	37	1,135,834	30.5
Expansion	502,643	49.4	515,214	62.8	110,854	19.4	42	2,359,277	63.4
BMK /d	-	-	43,215	5.3	9,428	1.6	7	17,052	0.4
Working capital	76,561	7.4	76,283	9.3	94,156	16.5	44	180,993	4.9
Others	-	-	42,137	5.1	21,425	3.7	9	29,054	0.8
<b>Total</b>	<b>1,017,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>
<b>Size of Assistance (Won million)</b>									
Up to 50	203	0.0	689	0.0	543	0.1	25	1,203	0.0
50-100	684	0.0	924	0.1	856	0.1	24	1,872	0.1
100-300	2,260	0.2	4,123	0.5	2,637	0.5	19	5,453	0.1
300-1,000	21,164	2.2	14,459	1.8	8,165	1.4	24	18,579	0.5
1,000-2,000	38,262	3.8	26,643	3.3	17,719	3.1	23	254,846	6.9
Over 2,000	954,918	93.8	773,960	94.3	541,958	94.8	24	3,440,257	92.4
<b>Total</b>	<b>1,047,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>
<b>Duration</b>									
Up to 1 year	30,243	3.0	41,279	5.0	34,149	6.0	9	42,330	1.1
1-4 years	21,963	2.2	83,666	10.2	167,728	29.3	40	260,892	7.0
4-8 years	294,058	38.7	254,324	31.0	180,787	31.6	46	1,545,547	41.5
8-10 years	199,186	9.7	185,109	22.6	119,654	20.9	26	1,123,029	30.2
10-15 years	452,670	44.5	256,420	31.2	58,864	10.3	16	706,010	19.0
Over 15 years	19,371	1.9	-	-	10,696	1.9	2	44,402	1.2
<b>Total</b>	<b>1,017,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>
<b>Sectoral Distribution</b>									
Manufacturing Industries	525,768	51.7	711,513	86.7	478,594	83.7	108	2,663,297	71.6
Consumer goods	82,267	8.1	102,316	12.5	155,797	27.2	16	276,798	7.4
Intermediate goods	285,797	28.1	109,920	13.4	114,720	20.1	47	975,317	26.2
Capital goods	157,704	15.5	496,025	60.4	198,746	34.8	43	1,409,128	37.9
Other	-	-	3,252	0.4	9,331	1.6	2	2,054	0.1
Nonmanufacturing industries	491,723	48.3	109,285	13.3	93,284	16.3	31	1,058,913	28.4
<b>Total</b>	<b>1,017,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>
<b>Geographical Distribution</b>									
Seoul City	512,761	50.4	76,151	9.3	138,363	24.2	27	1,103,762	29.6
Busan City	38,345	3.8	63,258	7.7	18,799	3.3	7	63,222	1.7
Kyunggi Province	18,223	1.8	43,929	5.4	43,294	7.6	21	121,341	3.3
South Chungcheong Province	63,355	6.2	-	-	1,087	0.2	2	74,125	2.0
North Chungcheong Province	723	0.1	28,151	3.4	24,754	4.3	11	39,765	1.1
Kang Won Province	4,448	0.4	93,158	11.4	40,019	7.0	7	196,490	5.3
South Jeonra Province	90,487	8.8	55,354	6.7	99,281	17.4	10	405,697	10.9
North Jeonra Province	-	-	-	-	10,257	1.8	6	22,049	0.6
South Kyungsang Province	262,843	25.8	231,854	28.2	52,498	9.2	39	742,391	19.9
North Kyungsang Province	26,283	2.6	228,943	27.9	143,526	25.0	9	953,368	25.6
Che-ju Island	23	0.1	-	-	-	-	-	-	-
<b>Total</b>	<b>1,017,491</b>	<b>100.0</b>	<b>820,798</b>	<b>100.0</b>	<b>571,878</b>	<b>100.0</b>	<b>139</b>	<b>3,722,210</b>	<b>100.0</b>

/a Foreign exchange fluctuations and L/C guarantees are not reflected.

/b Includes foreign exchange fluctuations, L/C guarantees and guarantees transferred to the Readjustment Corporation.

/c Number of companies.

/d Balancing, modernization and replacement.

KOREA

THE KOREA DEVELOPMENT BANK

Summarized Income Statements for the Years 1976-79  
(Won million)

	1976	1977	1978	1979
<u>INCOME</u>				
Interest Income				
Interest on loans	67,218	89,599	138,684	233,394
Interest on bonds & debentures	1,254	1,807	2,409	2,858
Interest on deposits	312	2,102	2,462	3,186
Total Interest Income	68,784	93,508	143,555	239,438
Other Income				
Dividend income	3,718	5,572	5,748	12,399
Guarantee commissions	9,130	12,999	15,972	17,371
Capital gains on sale of investment	4,861	5,640	7,991	-
Other income	3,040	8,654	6,126	9,388
Total Other Income	20,749	32,865	35,837	39,158
Total Gross Income	89,533	126,373	179,392	278,596
<u>EXPENSES</u>				
Financial Expenses				
Interest on:				
Borrowings from Government	29,976	42,400	67,973	118,269
Foreign loans	7,977	13,530	20,175	44,246
Debentures	10,110	15,058	22,244	32,393
Deposits	4,284	5,270	4,989	6,211
Commission and others	1,215	513	2,252	4,929
Total Financial Expenses	53,562	76,771	117,633	206,048
Administrative and Other Expenses				
Personnel expenses	5,079	6,198	8,863	15,212
Provision for loan losses	2,725	622	3,604	7,678
Provision for foreign exchange losses (net)	2,501	6,032	11,829	3,295
Other expenses	2,971	4,204	3,986	5,329
Total Admin. & Other Expenses	13,276	17,056	28,282	31,514
Total Expenses	66,838	93,827	145,915	237,562
Net income before defense tax	22,695	32,546	33,477	41,034
Defense tax	1,555	2,201	2,297	3,570
NET INCOME /a	21,140	30,345	31,180	37,464

/a In terms of the provisions of the KDB Act, the entire net income of KDB is transferred to "Legal Reserves". The Government of Korea which is the sole shareholder of KDB does not receive any dividend.

KOREA

THE KOREA DEVELOPMENT BANK

Summarized Balance Sheets as of December 31, 1976-79  
(Won million)

	1976	1977	1978	1979
<u>ASSETS</u>				
<u>Current Assets</u>				
Cash and bank deposits	48,827	59,207	142,201	152,882
Securities	73,099	49,682	5,766	101,856
Short-term loans /a	n.a.	n.a.	n.a.	95,694
Current portion of loans	98,147	128,689	141,094	186,920
Accrued interest and other receivables	22,942	24,869	30,595	45,251
Other current assets	10,600	20,355	14,393	42,998
<u>Total Current Assets</u>	<u>253,615</u>	<u>282,802</u>	<u>334,049</u>	<u>625,601</u>
<u>Long-Term Loans</u>				
Domestic currency loans:				
Working capital loans	75,402	107,176	115,089	141,885
Capital loans	589,890	795,395	1,124,245	1,577,001
<u>Total Domestic Currency Loans</u>	<u>665,292</u>	<u>902,571</u>	<u>1,239,334</u>	<u>1,718,886</u>
(Current portion thereof)	(90,821)	(120,139)	(93,503)	(121,791)
Foreign currency loans	74,601	105,328	204,142	323,457
(Current portion thereof)	(7,326)	(8,550)	(47,591)	(65,129)
<u>Total Loans</u>	<u>739,893</u>	<u>1,007,899</u>	<u>1,443,476</u>	<u>2,042,343</u>
(Less: Current portion)	(98,147)	(128,689)	(141,094)	(186,920)
<u>Net Long-term Loans</u>	<u>641,746</u>	<u>879,210</u>	<u>1,302,382</u>	<u>1,855,423</u>
<u>Investments</u>				
Equity shares	160,238	217,362	273,516	300,391
Debentures	17,527	23,235	26,384	31,791
<u>Total Investments</u>	<u>177,765</u>	<u>240,597</u>	<u>299,900</u>	<u>332,182</u>
<u>Other Assets</u>				
Property and equipment	6,305	6,550	7,292	9,559
Receivables from loan, investment and property disposal	26,328	24,672	27,420	28,946
Other assets	6,428	8,503	27,464	26,732
<u>Total Other Assets</u>	<u>35,877</u>	<u>34,791</u>	<u>61,067</u>	<u>55,678</u>
<u>Total Assets</u>	<u>1,109,003</u>	<u>1,437,400</u>	<u>1,997,398</u>	<u>2,868,884</u>

/a Included in working capital loans for 1976-78.

	1976	1977	1978	1979
<u>LIABILITIES AND EQUITY</u>				
<u>Current Liabilities</u>				
Short-term deposits	24,038	61,645	105,048	107,105
Current portion of long-term debt	55,272	101,569	124,422	170,195
Credit control account	15,380	36,879	19,506	16,116
Other current liabilities	15,915	17,797	27,990	53,073
<u>Total Current Liabilities</u>	<u>110,605</u>	<u>217,890</u>	<u>276,966</u>	<u>346,489</u>
<u>Long-Term Liabilities</u>				
<u>Special Finance Debentures</u>	21,312	15,969	10,709	5,507
Deduct: Equivalent cash deposits /a	(21,312)	(15,969)	(10,709)	(5,507)
Net liability for SFD	-	-	-	-
<u>Time Deposits</u>				
Domestic currency	-	6,900	13	3,503
Foreign currency	20,984	11,172	-	544
<u>Total Time Deposits</u>	<u>20,984</u>	<u>18,072</u>	<u>13</u>	<u>4,047</u>
<u>Foreign Currency Borrowings</u>				
Official sources	66,363	100,416	146,048	178,261
Commercial sources /b	118,729	162,572	241,237	624,915
	185,092	262,988	387,285	803,176
(Less: Current portion)	(16,324)	(22,968)	(33,865)	(38,752)
<u>Net Foreign Currency Borrowings</u>	<u>168,768</u>	<u>240,020</u>	<u>353,420</u>	<u>764,424</u>
<u>Domestic Currency Borrowings</u>				
Government of Korea	168,590	202,185	262,505	311,936
Industrial Rationalization Fund	51,111	51,111	50,078	47,607
Tourism Development Fund	350	4,760	15,324	24,069
National Investment Fund	207,198	298,280	537,182	809,125
IFDs in domestic currency	57,340	79,514	95,571	143,189
	484,589	635,850	960,660	1,335,926
(Less: Current portion)	(38,948)	(78,601)	(90,557)	(131,442)
<u>Net Domestic Currency Borrowings</u>	<u>445,641</u>	<u>557,249</u>	<u>870,103</u>	<u>1,204,484</u>
<u>Provisions for Doubtful Accounts</u>	12,847	13,500	17,000	24,702
<u>Other Long-Term Liabilities</u>	13,670	18,836	25,068	32,446
<u>Total Long-Term Liabilities</u>	<u>661,910</u>	<u>847,677</u>	<u>1,265,604</u>	<u>2,030,103</u>
<u>Total Liabilities</u>	<u>772,522</u>	<u>1,065,567</u>	<u>1,542,570</u>	<u>2,376,592</u>
<u>Equity</u>				
Paid-in capital	274,942	279,942	331,757	331,757
Reserves and retained earnings	61,546	91,891	123,071	160,535
<u>Total Equity</u>	<u>336,488</u>	<u>371,833</u>	<u>454,828</u>	<u>492,292</u>
<u>Outstanding Guarantees</u>				
Domestic currency	58,156	71,314	92,739	141,420
Foreign currency	2,453,537	3,207,530	3,805,599	3,580,790
<u>Total Guarantees</u>	<u>2,511,693</u>	<u>3,278,844</u>	<u>3,898,338</u>	<u>3,722,210</u>
Deduct: Customers' liabilities for guarantees	2,511,693	3,278,844	3,898,338	3,722,210
Net liabilities for guarantees	-	-	-	-
<u>Total Liabilities and Equities</u>	<u>1,109,003</u>	<u>1,437,400</u>	<u>1,997,398</u>	<u>2,868,884</u>

/a Fixed deposit against outstanding balance of special finance debentures which can only be used for the redemption of these debentures.

/b Including IFDs in foreign currency.

ANNEX B  
Table 15

KOREA

THE KOREA DEVELOPMENT BANK

Cash Flow Statements, 1976-79  
(Won million)

	1976	1977	1978	1979
<b>Sources of Funds</b>				
Net income	21,140	30,345	31,180	37,464
Noncash charges	2,853	796	3,656	18,249
Increase in paid-in capital	71,742	5,000	51,815	-
Capital transfer from Government	-	-	-	-
Drawdown on foreign currency borrowings:				
Official sources	33,471	39,472	52,722	53,273
Commercial sources (excl. IFDs in foreign currency)	43,176	21,117	65,316	400,634
Subtotal	<u>76,647</u>	<u>60,589</u>	<u>118,038</u>	<u>453,907</u>
Borrowing from:				
GOK	23,800	41,209	64,330	83,262
NIF	92,078	99,759	256,055	310,754
IRF	-	-	-	-
TDF	-	4,443	10,788	9,830
Subtotal	<u>115,878</u>	<u>145,411</u>	<u>331,173</u>	<u>403,846</u>
Issuance of IFDs				
In domestic currency	33,264	46,878	55,417	62,279
In foreign currency	35,968	35,149	29,544	17,763
Subtotal	<u>69,232</u>	<u>82,027</u>	<u>84,961</u>	<u>80,042</u>
Increase in deposits	(4,151)	56,194	7,971	1,715
Sale of investments /a	13,014	9,026	27,716	3,576
Collection of loans				
Domestic currency	58,010	67,524	129,466	175,061
Foreign currency	5,905	9,624	14,260	70,027
Subtotal	<u>63,915</u>	<u>77,148</u>	<u>143,726</u>	<u>245,088</u>
Increase in other liabilities /b	3,938	7,048	16,425	22,404
<b>Total Sources</b>	<u>434,208</u>	<u>473,584</u>	<u>816,661</u>	<u>1,266,291</u>
<b>Uses of Funds</b>				
Increase in property & equipment	1,040	388	898	2,480
Loan disbursements:				
Domestic currency	194,466	304,802	466,228	750,308
Foreign currency	29,951	34,807	95,778	189,342
Subtotal	<u>224,417</u>	<u>339,609</u>	<u>562,006</u>	<u>939,650</u>
Adjustment of foreign exchange gains (losses)	1,571	5,545	17,296	(9,404)
New investment	45,660	71,858	87,019	35,858
Repayments against domestic currency borrowings:				
GOK	4,284	7,614	4,009	33,832
NIF	1,710	8,676	17,153	38,811
IRF	-	-	1,033	2,471
TDF	30	34	224	1,085
Subtotal	<u>6,024</u>	<u>16,324</u>	<u>22,419</u>	<u>76,199</u>
Repayments against foreign currency borrowings:				
Official sources	3,213	5,419	7,090	21,060
Commercial sources	25,242	12,423	16,195	18,008
Subtotal	<u>28,455</u>	<u>17,842</u>	<u>23,285</u>	<u>39,068</u>
Redemption of IFDs				
In domestic currency	44,444	24,704	39,360	14,661
In foreign currency	-	-	-	16,708
Subtotal	<u>44,444</u>	<u>24,704</u>	<u>39,360</u>	<u>31,369</u>
Increase in securities	66,082	(23,417)	(43,916)	96,090
Increase in other assets /c	2,273	10,351	19,804	44,300
Increase in cash	14,242	10,380	82,994	10,681
<b>Total Uses</b>	<u>434,208</u>	<u>473,584</u>	<u>816,661</u>	<u>1,266,291</u>

/a Excluding capital gains.

/b Including other current liabilities and other long-term liabilities.

/c Including accrued interest and fees, other current assets, other long-term assets, and receivables from property disposal.

ANNEX B  
Table 16

KOREA

THE KOREA DEVELOPMENT BANK

Indicators of Financial and Operational Performance, 1976-79  
(Won million)

	1976	1977	1978	1979
<u>Total Assets</u>	1,109,010	1,437,400	1,997,398	2,868,884
Of which:				
Loan portfolio <u>/a</u>	739,893	1,007,277	1,443,476	2,138,037
Investment portfolio	177,765	240,597	299,900	332,182
<u>Long-term Liabilities &amp; guarantees</u>	3,173,602	4,126,521	5,163,942	5,752,313
Of which:				
In foreign currency	185,092	274,000	387,285	803,176
Borrowings from Government	168,590	202,185	262,505	311,936
Debentures in domestic currency	57,340	79,514	95,571	143,189
Special loans and funds	258,659	354,151	602,584	880,801
Deposits	20,991	18,072	13	4,047
<u>Outstanding guarantees</u>	2,511,692	3,278,844	3,898,338	3,722,210
Of which: Covered under GRA <u>/a</u>	2,072,632	2,538,312	2,968,636	2,707,197
<u>Equity</u>	336,488	371,833	454,828	492,292
<u>Financial Performance</u>				
<u>Percentage of Average Total Assets</u>				
1. Gross income	9.2	9.9	10.4	11.5
2. Financial expenses	5.5	6.0	6.8	8.5
3. Gross spread (1-2)	3.7	3.9	3.6	3.0
4. Administrative expenses	0.8	0.8	0.7	1.0
5. Provisions for doubtful loans & foreign exchange losses	0.3	0.5	0.9	0.5
6. Income tax	-	-	-	-
7. Profit before provision	2.5	2.9	2.7	2.0
8. Net profit	2.2	2.4	1.8	1.5
<u>Net Profit as % of Average Net Worth <u>/b</u></u>	7.3	8.6	7.5	7.9
<u>Other Ratios <u>/c</u></u>				
1. Provisions & reserves as % of total portfolio	9.1	8.4	8.0	7.4
2. Book value as % of par value	122	133	137	148
3. Debt service cover ratio (times)	1.43	1.31	1.42	1.31
4. Interest cover ratio (times)	1.47	1.23	1.24	1.13
5. Cost of total long-term resources as % of average total long-term resources	6.0	6.0	6.5	9.2
6. Income from loan portfolio as % of average loan portfolio <u>/d</u>	10.2	10.7	11.8	12.5
7. Interest on long-term debt as % of average long-term debt	9.0	9.5	10.2	10.2
8. Spread (6-7)	1.2	1.2	1.6	2.3
9. Long-term debt/equity ratio <u>/e</u>	2.9	4.3	4.8	6.3
10. Total debt/equity ratio <u>/e</u>	3.6	4.9	5.4	7.2
11. Total debt/equity ratio <u>/f</u>	10.0	11.7	12.0	12.8
12. Debt equity/ratio according to KDB Act, Article 25 <u>/g</u>	7.9	9.5	9.1	8.1
13. Current ratio	2.0	1.3	1.2	1.8/h

/a Guarantee Release Agreement under which the Government covers the risk of KDB.

/b Net income after National Defense Tax: KDB is not subject to income/corporate tax.

/c Including unappropriated profits.

/d Based on a daily average.

/e Excluding guarantees covered under GRA.

/f Including guarantees covered under GRA.

/g Debt principally comprises not-government-guaranteed IPDs and guarantee outstanding.

/h On comparable data base: Around 1.5.



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THE KOREA DEVELOPMENT BANK

Portfolio Status (Arrears, Reschedulings, Write-offs), 1976-78  
(Won million)

As of December 31	1976	1977	1978	1979
<u>A. Loan Portfolio in Arrears</u>				
(Total loans outstanding)	(739,893)	(1,007,277)	(1,443,476)	(2,138,037)
<u>1. Arrears</u>				
Principal in arrears	573	1,215	2,270	3,488/a
Interest in arrears	351	730	1,766	9,046/a
<u>Total Arrears</u>	<u>924</u>	<u>1,945</u>	<u>4,036</u>	<u>12,534/a</u>
(As % of total loans outstanding)	(0.1)	(0.2)	(0.3)	(0.6)
<u>Principal Affected by Arrears</u>	<u>6,561</u>	<u>15,038</u>	<u>36,090</u>	<u>123,713/a</u>
(as % of total principal outstanding)	(0.9)	(1.5)	(2.5)	(5.8)
<u>2. Loan Reschedulings</u>				
Principal amount rescheduled	48,723	42,036	45,190	58,852/a
(Of which due at the time of rescheduling)	(14,889)	(12,074)	(14,548)	(16,071)
Reschedulings as % of outstanding portfolio	6.6	4.2	3.1	2.8
<u>3. Loans Transferred to RAC</u>	1,530	1,025	3,506	1,856
Principal affected				
<u>4. Amounts Written-Off</u>	n.a.	-	169	-
<u>5. Loan Portfolio Affected (%)</u>				
By arrears, reschedulings, transfer to RAC and writeoffs	<u>7.7</u>	<u>5.8</u>	<u>5.9</u>	<u>8.6</u>
<u>6. Collection Performance</u>				
Collection rate (%)	98.6	98.8	98.6	97.4
<u>B. Guarantee Portfolio in Arrears</u>				
(Total guarantees outstanding)	(2,511,692)	(3,278,844)	(3,898,338)	(3,722,210)
<u>Arrears</u>				
Principal in arrears	-	2,071	2,285	6,945
Fees in arrears	1	24	52	268
<u>Total Arrears</u>	<u>1</u>	<u>2,095</u>	<u>2,337</u>	<u>7,213</u>
(As % of total guarantees outstanding)	-	(0.1)	(0.1)	(0.2)
<u>Outstanding Guarantees Affected by Arrears</u>	<u>80</u>	<u>12,952</u>	<u>5,784</u>	<u>52,080</u>
(As % of guarantees portfolio)	-	(0.4)	(0.2)	(1.4)

/a Inconsistent with audit report.

KOREA  
THE KOREA DEVELOPMENT BANK

Analysis of Loans in Arrears, 1977-79

(Won million)

As of December 31	1977				1978				1979			
	<u>Portfolio affected</u> No./a	<u>Amount</u>	<u>Amount in arrears</u>		<u>Portfolio affected</u> No./a	<u>Amount</u>	<u>Amount in arrears</u>		<u>Portfolio affected</u> No./a	<u>Amount</u>	<u>Amount in arrears</u>	
			Principal	Interest			Principal	Interest			Principal	Interest
I. <u>Length of Arrears</u>												
Less than 3 months	24	10,744	793	365	36	26,257	1,128	998	46	53,726	2,316	3,329
3-6 months	8	3,233	208	132	1	2,509	520	364	6	49,136	961	3,158
6-12 months	1	11	2	2	4	6,435	479	335	6	14,543	126	2,203
1-2 years	1	761	226	239	3	889	143	69	2	6,308	85	356
<u>Total</u>	<u>34</u>	<u>14,749</u>	<u>1,229</u>	<u>738</u>	<u>44</u>	<u>36,090</u>	<u>2,270</u>	<u>1,766</u>	<u>60</u>	<u>123,713</u>	<u>3,488</u>	<u>9,046</u>
II. <u>Sector</u>												
Government	-	-	-	-	-	-	-	-	-	-	-	-
Private	34	14,749	1,229	738	44	36,090	2,270	1,766	60	123,713	3,488	9,046
<u>Total</u>	<u>34</u>	<u>14,749</u>	<u>1,229</u>	<u>738</u>	<u>44</u>	<u>36,090</u>	<u>2,270</u>	<u>1,766</u>	<u>60</u>	<u>123,713</u>	<u>3,488</u>	<u>9,046</u>
III. <u>Type of Industry</u>												
A. <u>Manufacturing Industries</u>												
Textiles, wearing apparel and leather	3	1,476	148	101	8	6,497	1,204	519	9	22,353	158	2,284
Chemicals, rubber and plastic	3	3,269	97	29	2	1,967	38	5	10	4,523	605	244
Petroleum, coal & nonmetallic mineral products	1	245	32	14	4	3,668	101	45	1	294	112	89
Basic metals	2	270	22	11	7	4,631	174	312	7	14,296	999	692
Fabricated metal products, machinery	-	-	-	-	3	3,623	152	106	7	51,213	1,335	3,050
Electrical equipment	1	444	6	11	3	2,101	58	25	2	456	-	24
Transport equipment	1	244	7	5	6	4,065	18	112	2	2,473	-	104
Others	3	3,624	466	318	-	-	-	-	2	311	24	9
Subtotal Manufacturing	<u>14</u>	<u>9,577</u>	<u>778</u>	<u>489</u>	<u>33</u>	<u>26,552</u>	<u>1,745</u>	<u>1,124</u>	<u>40</u>	<u>95,919</u>	<u>3,233</u>	<u>6,496</u>
B. <u>Nonmanufacturing Industries</u>												
Agriculture, forestry & fishery	2	2,981	380	175	-	-	-	-	1	9,702	-	1,924
Electricity, gas & waterworks	-	-	-	-	-	-	-	-	1	241	-	7
Construction	1	1,229	-	25	-	-	-	-	-	-	-	-
Transportation	12	281	21	14	15	7,352	361	432	13	16,004	201	548
Hotel & tourism	5	681	50	37	6	2,186	164	210	5	1,847	54	71
Subtotal Nonmanufacturing	<u>20</u>	<u>5,172</u>	<u>451</u>	<u>251</u>	<u>21</u>	<u>9,538</u>	<u>525</u>	<u>642</u>	<u>20</u>	<u>27,794</u>	<u>255</u>	<u>2,550</u>
<u>Grand Total</u>	<u>34</u>	<u>14,749</u>	<u>1,229</u>	<u>738</u>	<u>44</u>	<u>36,090</u>	<u>2,270</u>	<u>1,766</u>	<u>60</u>	<u>123,713</u>	<u>3,488</u>	<u>9,046</u>

/a Number of companies.

AEP Projects Department  
June 1, 1980

ANNEX B  
Table 18

KOREA

THE KOREA DEVELOPMENT BANK

Resource Position as of December 31, 1979

<u>A. DOMESTIC CURRENCY RESOURCES</u>		(Won million)
<u>1. Long-Term Resources</u>		
(a) <u>Raised in Domestic Currency</u>		
Equity:		
Paid-in capital		331,757
Reserves and retained earnings		160,535
Subtotal		<u>492,292</u>
Borrowings:		
Government		311,936
Industrial Rationalization Fund		47,607
National Investment Fund		809,125
Tourism Development Fund		24,069
Subtotal		<u>1,192,737</u>
Debentures		143,189
Revolving Funds		10,652
Time deposits (more than 1 year)		3,503
Subtotal		<u>157,344</u>
(b) <u>Raised in Foreign Currency /a</u>		
Debentures		57,005
Syndicated bank loans		264,275
Time deposits		280
Subtotal		<u>321,560</u>
		(663,010)/b
<u>Total Long-Term Resources in Domestic Currency</u>		<u>2,163,933</u>
Less:		
Term loans outstanding in domestic currency		1,718,886
Investments outstanding		332,182
Receivables from property disposed		28,946
Fixed assets		9,559
Other assets		26,732
Subtotal		<u>2,116,305</u>
Resources available for disbursement		47,628
Less undisbursed commitments		-
<u>Resources Available for Commitment</u>		<u>47,628</u>

/a All these resources, which were raised in foreign currency have been or are intended to be used in domestic currency (based on contracted amounts net of repayments).

/b Amounts in parenthesis: US\$ thousand.

(Won million)

<b>2. <u>Short-Term Resources</u></b>	
Short-term deposits	107,105
Others	69,189
<u>Total Short-Term Resources</u>	<u>176,294</u>
Less operating loans (less than 12 months)	95,694
<u>Short-Term Resources Available for Disbursement and Commitments</u>	<u>80,600</u>
<b>B. <u>FOREIGN CURRENCY RESOURCES</u></b>	
<b>1. <u>Borrowings from Official Sources</u></b>	
IBRD	121,398
AID	5,000
ADB	77,186
KfW	11,348
Less revolving funds	10,652
Subtotal	<u>204,280</u> (421,196) /b
<b>2. <u>Borrowings from Commercial Sources</u></b>	
IFDs	53,874
Syndicated bank loans	249,761
Subtotal	<u>303,635</u> /c (626,052)
<b>3. <u>Time Deposits</u></b>	
	<u>544</u>
<u>Total Foreign Currency Resources</u>	<u>508,459</u> (1,048,369) /b
Less: Foreign currency loans outstanding	323,457
Requirements against foreign deposits received	150
Foreign currency resources available for disbursement	184,572
Less: Undisbursed commitments	16,043
Foreign currency resources available for commitment	168,529
Less: Uncommitted approvals	2,110
<u>Foreign Currency Resources Available for Approval</u>	<u>166,699</u>

/b Amounts in parenthesis: US\$ thousand.

/c Portion which is intended to be used in foreign currency lending operations.

KOREA

THE KOREA DEVELOPMENT BANK

Foreign Currency Long-Term Borrowings as of December 31, 1979  
(Each currency in thousand)

A. Official Sources

	Contract amount	Approvals /a	Commitments /a	Disbursements	Repayments /b	Outstanding /c	Interest rate (%)		Maximum term /d		Date of signing
							Borrowing	Relending	For KDB	For borrowers	
<u>IBRD</u>											
1st loan	US\$ 60,000	US\$ 60,000	US\$ 60,000	US\$ 60,000	US\$ 8,794	US\$ 51,206	8.5	10.5	18(3)	18(3)	03/31/75
2nd loan	82,500	80,664	80,664	79,204	4,836	74,368	8.7	10.7	17(3)	35(5)	12/23/76
KECO	11,713	11,713	11,713	11,713	0	11,713	5.83	7.5	25(7)	17(3)	11/20/76
3rd loan	110,000	97,701	97,701	50,599	277	50,322	7.5	9.5	17(3)	15(3)	06/21/78
Subtotal	264,213	250,078	250,078	201,516	13,907	187,609					
<u>ADB</u>											
1st loan	US\$ 10,000	US\$ 10,000	US\$ 10,000	US\$ 10,000	US\$ 5,768	US\$ 4,232	7.5	10	15(3)	15(3)	11/23/70
2nd loan	20,000	20,000	20,000	20,000	9,648	10,352	7.5	9.5	15(3)	15(3)	12/15/72
3rd loan	30,000	30,000	30,000	30,000	10,565	19,435	7.5-8.75	9.5-10.75	15(3)	15(3)	03/20/74
HII loan	17,416	17,416	17,416	17,416	997	16,419	8.75	10.5	15(4)	15(4)	05/30/75
4th loan	40,000	40,000	40,000	40,000	1,993	38,007	8.75	10.75	15(3)	15(3)	12/12/75
5th loan	50,000	35,487	35,487	27,180	0	27,180	7.65	9.65	15(3)	15(3)	04/13/78
Subtotal	167,416	152,903	152,903	144,596	28,971	115,625					
<u>AID</u>											
1st loan	US\$ 5,000	US\$ 4,998	US\$ 4,998	US\$ 4,998	US\$ 4,998	US\$ 0	5	8	10(2.5)	10(2.5)	04/12/60
2nd loan	11,374	11,374	11,374	11,374	6,910	4,464	5	8	15(3)	15(3)	11/19/66
3rd loan	11,000	11,000	11,000	11,000	5,155	5,845	6	10	15(3)	15(3)	06/26/68
Subtotal	27,374	27,372	27,372	27,372	17,063	10,309					
<u>KFW</u>											
1st loan	DM 20,000	DM 20,000	DM 20,000	DM 20,000	DM 12,464	DM 7,536	5	8	20(5)	10(2)	01/24/66
2nd loan	10,000	9,998	9,998	9,998	9,408	590	8	10	10(2)	10(2)	10/14/70
3rd loan	10,000	10,000	10,000	10,000	0	10,000	7	9	30(10)	15(3)	11/12/73
4th loan	20,000	14,832	14,832	14,832	0	14,832	7	9	30(10)	15(3)	08/04/76
Subtotal	60,000	54,830	54,830	54,830	21,872	32,958					

B. Commercial Sources

	Contract amount	Disbursements	Repayments /b	Outstanding /c	Borrowing rate (%)	Maximum term /d (for KDB)	Date of signing
<u>Bank Loans</u>							
1st loan	US\$ 25,000	US\$ 25,000	US\$ 25,000	US\$ 0	6 mos Libor+1.75	5(3)	06/09/70
2nd loan	US\$ 80,000	US\$ 80,000	US\$ 32,000	US\$ 48,000	6 mos Libor+1	10(3)	01/24/74
3rd loan	US\$ 80,000	US\$ 80,000	US\$ 45,588	US\$ 34,412	6 mos Libor+1.875	5(2)	06/25/76
4th loan	Y 5,000,000	Y 5,000,000	Y 550,000	Y 4,450,000	9.9	7(3)	07/21/76
5th loan	US\$ 250,000	US\$ 250,000	US\$ 0	US\$ 250,000	6 mos Libor+0.875	10(3)	05/31/78
6th loan	Y 28,000,000	Y 28,000,000	Y 1,400,000	Y 26,600,000	7.8	10	05/31/79
7th loan	US\$ 600,000	US\$ 600,000	US\$ 0	US\$ 600,000	First 5 years 6(3) mos Libor+0.625	10(3)	07/05/79
					Remaining 5 years 6(3) mos Libor+0.75		
<u>Eurobonds</u>							
1st issue	DH 75,000	DH 75,000	DH 0	DH 75,000	8.5	15(5)	10/10/74
2nd issue	DH 60,000	DH 60,000	DH 0	DH 60,000	9.5	5	04/20/76
3rd issue	US\$ 10,000	US\$ 10,000	US\$ 10,000	US\$ 0	9.25	3	07/15/76
4th issue	KD 7,000	KD 7,000	KD 7,000	KD 0	8.75	3	10/16/76
5th issue	US\$ 25,000	US\$ 25,000	US\$ 0	US\$ 25,000	9.5	5	12/08/76
6th issue	US\$ 25,000	US\$ 25,000	US\$ 0	US\$ 25,000	9.5	5	02/15/77
7th issue	DM 100,000	DM 100,000	DM 0	DM 100,000	7.25	7	11/25/77
8th issue	Y 10,000,000	Y 10,000,000	Y 0	Y 10,000,000	6.7	10(5)	01/20/78
9th issue	KD 12,000	KD 12,000	KD 0	KD 12,000	7.875	10	03/10/79

- /a Net of cancellations.  
/b To lending institutions.  
/c With lending institutions.  
/d Grace period in parenthesis.

KOREA

THE KOREA DEVELOPMENT BANK

Forecast of Approvals, Commitments and Disbursements, 1980-83  
(Won million)

	1980	1981	1982	1983
<u>Approvals</u>				
Domestic currency				
Capital loan	713,198	813,045	926,872	1,056,634
Working capital loan	178,299	203,261	231,718	264,158
Subtotal	<u>891,497</u>	<u>1,016,306</u>	<u>1,158,590</u>	<u>1,320,792</u>
Foreign currency loan	239,392	272,907	311,114	354,670
<u>Total Loan Approvals</u>	<u>1,130,889</u>	<u>1,289,213</u>	<u>1,469,704</u>	<u>1,675,462</u>
<u>Equity Investments</u>	<u>56,500</u>	<u>70,200</u>	<u>84,240</u>	<u>101,088</u>
<u>Issuance of Guarantees</u>				
Domestic currency	65,446	73,276	81,107	88,938
Foreign currency	<u>1,570,699</u>	<u>1,758,631</u>	<u>1,946,569</u>	<u>2,134,504</u>
<u>Total New Guarantees</u>	<u>1,636,145</u>	<u>1,831,907</u>	<u>2,027,676</u>	<u>2,223,442</u>
<u>Commitments</u>				
Domestic currency				
Capital loan	713,198	813,045	926,872	1,056,634
Working capital loan	178,299	203,261	231,718	264,158
Subtotal	<u>891,497</u>	<u>1,016,306</u>	<u>1,158,590</u>	<u>1,320,792</u>
Foreign currency loan	234,604	267,449	304,892	347,577
<u>Total Commitments</u>	<u>1,126,101</u>	<u>1,283,755</u>	<u>1,463,482</u>	<u>1,668,369</u>
<u>Disbursements</u>				
Domestic currency				
Capital loan	713,198	813,045	926,872	1,056,634
Working capital loan	178,299	203,261	231,718	264,158
Subtotal	<u>891,497</u>	<u>1,016,306</u>	<u>1,158,590</u>	<u>1,320,792</u>
Foreign currency loan	222,874	254,077	289,647	330,198
<u>Total Disbursements</u>	<u>1,114,371</u>	<u>1,270,383</u>	<u>1,448,237</u>	<u>1,650,990</u>

Basic Assumption:

1. Approvals, commitments and disbursements are expected to increase annually by 14%, except for 1980 because of the exchange rate adjustment.
2. Foreign currency loans are expected to account for 20% of domestic currency loans and working capital loans for 20% of total loans..
3. Commitments and disbursements: 100% of each year's domestic currency and 98% of foreign currency loan approvals are expected to be committed during the same year; 100% of each year's domestic currency and 95% of foreign currency loan commitments will be disbursed.

KOREA

THE KOREA DEVELOPMENT BANK

Projected Income Statements, 1980-83  
(Won million)

	1980	1981	1982	1983
<u>INCOME</u>				
<u>Interest Income</u>				
Interest on loans	401,712	550,379	695,247	837,554
Interest on bonds & debentures	4,158	4,898	5,502	6,107
Interest on deposits	7,000	7,500	8,000	8,500
<u>Total Interest Income</u>	<u>412,870</u>	<u>562,777</u>	<u>708,749</u>	<u>852,161</u>
<u>Other Income</u>				
Dividend income	14,713	18,839	23,279	28,185
Guarantee commissions	20,992	24,772	27,568	30,365
Capital gains on sale of investment	600	700	800	900
Other income	11,976	13,772	15,837	18,213
<u>Total Other Income</u>	<u>48,281</u>	<u>58,083</u>	<u>67,484</u>	<u>77,663</u>
<u>Total Gross Income</u>	<u>461,151</u>	<u>620,860</u>	<u>776,233</u>	<u>929,824</u>
<u>EXPENSES</u>				
<u>Financial Expenses</u>				
Interest on:				
Borrowings from Government	193,043	263,749	330,482	392,918
Foreign loans	110,584	153,406	193,483	231,049
Debentures	52,797	81,821	105,903	133,893
Deposits	8,966	8,792	9,650	10,594
Commissions and others	5,800	6,961	8,353	10,023
<u>Total Financial Expenses</u>	<u>371,190</u>	<u>514,729</u>	<u>647,871</u>	<u>778,477</u>
<u>Administrative and Other Expenses</u>				
Personnel expenses	24,045	31,258	40,635	52,826
Provision for loan losses	9,245	9,637	10,630	11,712
Provision for foreign exchange losses	9,362	9,887	10,641	12,150
Other expenses	5,893	7,072	8,486	10,183
<u>Total Admin &amp; Other Expenses</u>	<u>48,545</u>	<u>57,854</u>	<u>70,392</u>	<u>86,871</u>
<u>Total Expenses</u>	<u>419,735</u>	<u>572,583</u>	<u>718,263</u>	<u>865,348</u>
Net income before defense tax	41,416	48,277	57,970	64,476
Defense tax	4,142	4,828	5,797	6,448
<u>NET INCOME</u>	<u>37,274</u>	<u>43,449</u>	<u>52,173</u>	<u>58,028</u>

KOREA

THE KOREA DEVELOPMENT BANK

Projected Balance Sheets, 1980-1983  
(Won million)

Year ending December 31	1980	1981	1982	1983
<u>ASSETS</u>				
<u>Current Assets</u>				
Cash and bank deposits	160,140	55,764	67,806	76,562
Securities	113,856	190,081	110,081	30,081
Short-term loans	110,839	127,170	145,382	165,939
Current portion of long-term loans	216,868	284,053	357,573	438,583
Accrued interest and guarantee fees receivable	37,020	40,722	44,794	49,274
Other current assets	32,049	35,163	38,591	42,366
<u>Total Current Assets</u>	<u>670,772</u>	<u>732,953</u>	<u>764,227</u>	<u>802,805</u>
<u>Long-Term Loans</u>				
Domestic currency loans:				
Operating loans (more than one year)	203,152	233,086	266,464	304,142
Capital loans	2,206,897	2,865,459	3,591,749	4,396,961
<u>Total Domestic Currency loans</u>	<u>2,410,049</u>	<u>3,098,545</u>	<u>3,858,213</u>	<u>4,701,103</u>
(Current portion thereof)	(154,483)	(200,582)	(251,422)	(307,787)
Foreign currency loans	567,139	758,831	965,007	1,189,054
(Current portion thereof)	(62,385)	(83,471)	(106,151)	(130,796)
<u>Total Loans</u>	<u>2,977,188</u>	<u>3,857,376</u>	<u>4,823,220</u>	<u>5,890,157</u>
(Less: Current portion)	(216,868)	(284,053)	(357,573)	(438,583)
<u>Net Loans</u>	<u>2,760,320</u>	<u>3,573,323</u>	<u>4,465,647</u>	<u>5,451,574</u>
<u>Investments</u>				
Equity shares	353,520	400,050	440,490	493,020
Debentures	39,280	44,450	49,610	54,780
<u>Total Investments</u>	<u>392,800</u>	<u>444,500</u>	<u>496,100</u>	<u>547,800</u>
<u>Other Assets</u>				
Property and equipment	9,353	9,481	9,986	10,927
Receivables from property disposal	26,878	26,689	26,520	26,368
Other assets	40,011	46,012	52,914	60,851
<u>Total Other Assets</u>	<u>75,533</u>	<u>81,493</u>	<u>88,751</u>	<u>97,494</u>
<u>Total Assets</u>	<u>3,899,425</u>	<u>4,832,269</u>	<u>5,814,725</u>	<u>6,899,673</u>



Year ending December 31,	1980	1981	1981	1983
<u>LIABILITIES AND EQUITY</u>				
<u>Current Liabilities</u>				
Short-term deposits	120,237	128,237	137,237	147,237
Current portion of long-term debt	265,927	293,722	367,928	391,007
Credit control account	33,103	42,982	53,876	65,954
Other current liabilities	63,067	95,528	75,414	118,077
<u>Total Current Liabilities</u>	<u>482,334</u>	<u>560,469</u>	<u>634,455</u>	<u>722,275</u>
<u>Long-Term Liabilities</u>				
<u>Time Deposits</u>				
Domestic currency	3,853	4,239	4,662	5,129
Foreign currency	706	765	832	903
<u>Total Time Deposits</u>	<u>4,559</u>	<u>5,004</u>	<u>5,494</u>	<u>6,032</u>
<u>Foreign Currency Borrowings</u>				
Commercial sources:				
Bank loans	933,727	1,239,815	1,529,359	1,812,359
Eurobonds	187,389	220,367	262,633	319,472
Subtotal	<u>1,121,116</u>	<u>1,460,182</u>	<u>1,791,992</u>	<u>2,131,831</u>
Official sources	236,118	256,649	295,311	328,508
(Less: Current portion)	(66,934)	(74,190)	(66,161)	(87,361)
<u>Net Foreign Currency Borrowings</u>	<u>1,290,300</u>	<u>1,642,641</u>	<u>2,021,142</u>	<u>2,372,978</u>
<u>Domestic Currency Borrowings</u>				
Government of Korea	381,778	458,394	545,535	644,828
Industrial Rationalization Fund	44,718	41,050	37,141	32,141
Tourism development fund	35,544	46,143	57,673	70,357
National investment fund	1,052,439	1,322,561	1,625,718	1,967,364
IFDs in domestic currency	<u>215,257</u>	<u>277,414</u>	<u>375,195</u>	<u>450,597</u>
	1,729,736	2,145,562	2,641,262	3,165,287
(Less: Current portion)	(198,993)	(219,532)	(301,767)	(303,646)
<u>Net Domestic Currency Borrowings</u>	<u>1,530,743</u>	<u>1,926,030</u>	<u>2,339,495</u>	<u>2,861,641</u>
Provisions for doubtful loans & investments	33,700	43,000	53,200	64,380
Provisions for foreign exchange losses	20,221	22,108	23,749	25,149
Other long-term liabilities	15,000	17,000	19,000	21,000
<u>Total Long-Term Liabilities (net of current portion)</u>	<u>2,894,523</u>	<u>3,655,783</u>	<u>4,462,080</u>	<u>5,351,180</u>
<u>Total Liabilities</u>	<u>3,376,857</u>	<u>4,216,252</u>	<u>5,096,535</u>	<u>6,073,455</u>
<u>Equity</u>				
Paid-in capital	331,757	381,757	431,757	481,757
Reserves and retained earnings	190,811	234,260	286,433	344,461
<u>Total Equity</u>	<u>522,568</u>	<u>616,017</u>	<u>718,190</u>	<u>826,218</u>
<u>Outstanding Guarantees</u>				
Domestic currency	93,494	104,680	115,867	127,054
Foreign currency	4,581,206	5,129,340	5,677,493	6,225,636
<u>Total Guarantees</u>	<u>4,674,700</u>	<u>5,234,020</u>	<u>5,793,360</u>	<u>6,352,690</u>
Deduct: Customers' liabilities for guarantees	(4,674,700)	(5,234,020)	(5,793,360)	(6,352,690)
Net liabilities for guarantees	-	-	-	-
<u>Total Liabilities and Equity</u>	<u>3,899,425</u>	<u>4,832,269</u>	<u>5,814,725</u>	<u>6,899,673</u>

ANNEX B  
Table 24

KOREA

THE KOREA DEVELOPMENT BANK

Projected Cash Flow Statements, 1980-83  
(Won million)

Years ending December 31	1980	1981	1982	1983
<u>Sources of Funds</u>				
Net income	37,274	43,449	52,173	58,028
Noncash charges	12,363	12,459	13,219	14,112
Increase in paid-in capital	-	50,000	50,000	50,000
Foreign currency borrowings from:				
Official sources	37,467	37,700	58,232	54,230
Commercial sources	348,000	348,000	348,000	348,000
Subtotal	<u>385,467</u>	<u>385,700</u>	<u>406,232</u>	<u>402,230</u>
Borrowings from:				
Government of Korea	83,222	95,705	110,061	126,570
National Investment Fund	295,900	340,285	391,328	450,027
Tourism Development Fund	13,080	15,042	17,298	19,893
Subtotal	<u>392,202</u>	<u>451,032</u>	<u>518,687</u>	<u>596,490</u>
Increase in deposits	7,405	8,445	9,490	10,538
Issuance of IFDs:				
In domestic currency	131,030	163,787	196,545	229,302
In foreign currency	58,000	58,000	58,000	58,000
Subtotal	<u>189,030</u>	<u>221,787</u>	<u>254,545</u>	<u>287,302</u>
Sale of investments	4,727	26,300	42,000	60,620
Loan collections	290,670	373,864	464,185	563,496
Sale of property and equipment	709	689	669	652
Sale of marketable securities	97,000	10,000	80,000	80,000
Increase in other liabilities	77,767	88,898	100,840	122,431
Decrease in other assets	1,500	1,851	2,036	2,239
Total Sources	<u>1,496,114</u>	<u>1,674,474</u>	<u>1,994,076</u>	<u>2,248,138</u>
<u>Uses of Funds</u>				
Increase in property & equipment	1,250	1,563	1,953	2,441
Loan disbursements:				
In domestic currency	891,497	1,016,306	1,158,590	1,320,792
In foreign currency	222,874	254,077	289,647	330,198
Subtotal	<u>1,114,371</u>	<u>1,270,383</u>	<u>1,448,237</u>	<u>1,650,990</u>
New investments	65,000	78,000	93,600	112,320
Repayment against:				
Domestic currency borrowings	70,460	97,363	120,768	147,867
Foreign currency borrowings	43,523	59,081	78,026	86,033
Official sources	(14,527)	(17,169)	(19,570)	(21,033)
Commercial sources	(28,996)	(41,912)	(58,456)	(65,000)
Subtotal	<u>113,983</u>	<u>156,444</u>	<u>198,794</u>	<u>233,900</u>
Redemption of IFDs				
In domestic currency	58,962	101,630	98,764	153,900
In foreign currency	3,209	25,022	15,734	1,161
Subtotal	<u>62,171</u>	<u>126,652</u>	<u>114,498</u>	<u>155,061</u>
Increase in marketable securities	90,000	86,225	-	-
Decrease in other liabilities	54,333	41,425	90,840	63,584
Increase in other assets	11,588	18,167	34,112	21,086
Total Uses	<u>1,512,696</u>	<u>1,778,859</u>	<u>1,982,034</u>	<u>2,239,382</u>
Cash increase (decrease) during the year	16,582	104,385	12,042	8,756
Cash balance at beginning of the year	176,722	160,149	55,764	67,806
Cash balance at end of the year	160,140	55,764	67,806	76,562

## KOREA

## THE KOREA DEVELOPMENT BANK

Projected Indicators of Financial and Operational Performance, 1980-83  
(Won million)

	1979	1980	1981	1982	1983
<b>Total Assets</b>	2,868,884	3,899,425	4,832,269	5,814,725	6,899,673
Of which:					
Loan portfolio	2,138,037	3,088,027	3,984,546	4,968,602	6,056,096
Investment portfolio	332,182	392,800	444,500	496,100	547,800
<b>Total long-term debts and guarantees</b>	5,752,313	7,569,223	8,889,803	10,255,440	11,703,870
Of which:					
In foreign currency	803,176	1,357,234	1,716,831	2,087,303	2,460,339
Borrowings from Government	311,936	381,778	458,394	545,535	644,828
Domestic currency IFDs	143,189	215,257	277,414	375,195	450,597
Special loans and funds	880,801	1,132,701	1,409,754	1,720,532	2,069,862
Deposits	4,047	4,559	5,004	5,494	6,032
<b>Outstanding guarantees</b>	3,722,210	4,674,700	5,234,020	5,793,360	6,352,690
Of which: Covered under GRA /b	2,707,197	3,600,828	4,031,661	4,462,509	4,893,350
<b>Equity</b>	492,292	522,568	616,017	718,190	826,218
<b>Financial Performance</b>					
<b>Percentage of Average Total Assets</b>					
1. Gross income	11.5	13.3	14.2	14.6	14.6
2. Financial expenses	8.5	10.7	11.8	12.2	12.2
3. Gross spread (1-2)	3.0	2.6	2.4	2.4	2.4
4. Administrative expenses	1.0	0.9	0.9	0.9	1.0
5. Provisions for doubtful loans & foreign exchange losses	0.5	0.5	0.4	0.4	0.3
6. Income tax	-	-	-	-	-
7. Profit before provision	2.0	1.6	1.4	1.4	1.3
8. Net profit	1.5	1.1	1.0	1.0	1.0
<b>Net Profit as % of Average Net Worth /b</b>	7.9	7.4	7.6	7.8	7.5
<b>Other Ratios</b>					
1. Provisions & reserves /c as % of total portfolio	7.4	7.9	7.5	7.3	7.2
2. Book value as % of par value	148	157	161	167	174
3. Debt service cover ratio (times)	1.3	1.3	1.2	1.3	1.3
4. Interest cover ratio (times)	1.1	1.1	1.1	1.1	1.1
5. Cost of total long-term resources as % of average total long-term resources	9.2	11.5	12.6	12.9	13.0
6. Income from loan portfolio as % of average loan portfolio	12.5	15.0	15.6	15.5	15.2
7. Interest on long-term debt as % of average long-term debt	10.2	13.2	14.3	14.6	14.6
8. Spread (6-7)	2.3	1.8	1.3	0.9	0.6
9. Long-term debt/equity ratio /d	6.3	7.6	7.9	8.1	8.2
10. Total debt/equity ratio /d	7.2	8.5	8.8	8.9	9.1
11. Total debt/equity ratio /e	12.8	15.4	15.3	15.2	15.0
12. Current ratio	1.8	1.4	1.3	1.2	1.1
13. Debt/equity ratio under KDB Act	8.1	8.7	8.2	7.8	7.4

/a Guarantee Release Agreement under which the Government covers the risk of KDB.

/b Net income after National Defense Tax: KDB is not subject to income/corporate tax.

/c Including unappropriated profits.

/d Excluding guarantees covered under GRA.

/e Including guarantees covered under GRA.

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THE KOREA DEVELOPMENT BANK

Estimated Commitments and Disbursements of Proposed Bank Loan /a  
(in US\$ million)

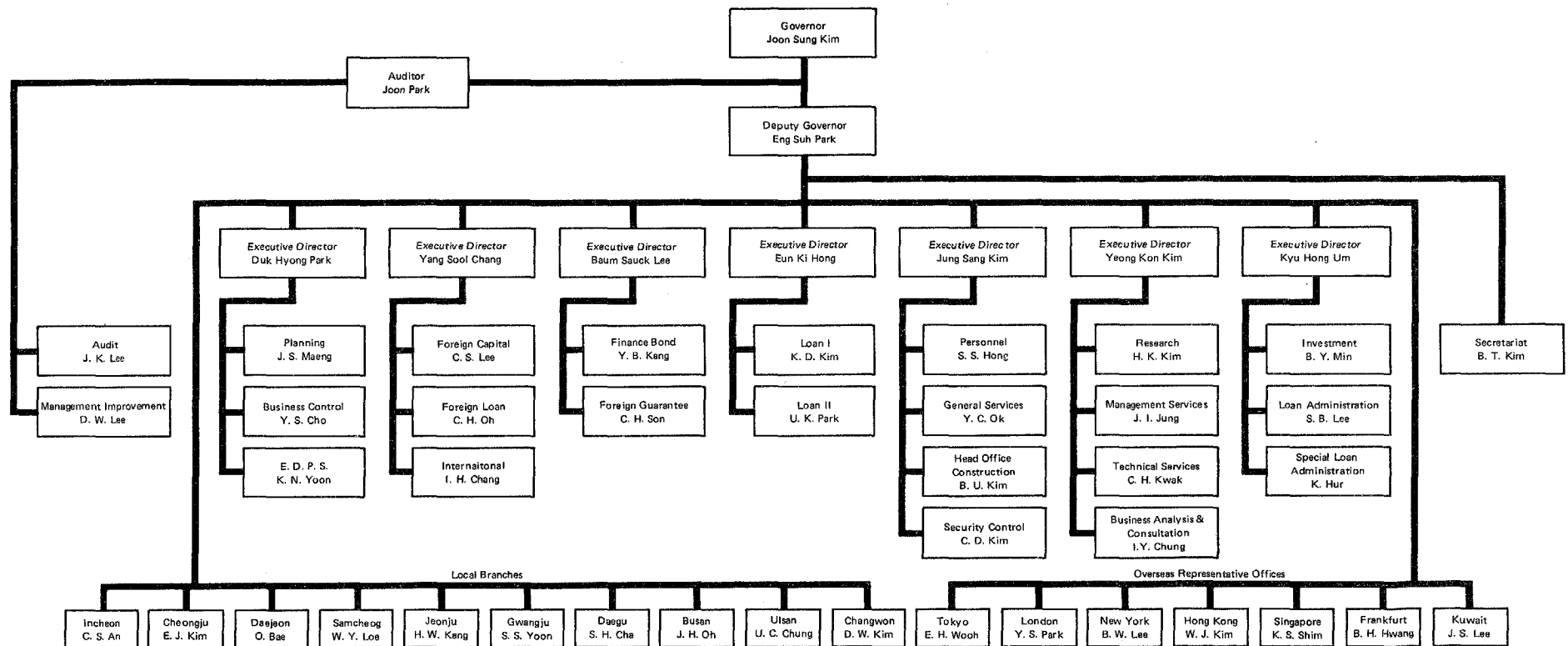
			<u>Commitments</u>		<u>Disbursements</u>	
			<u>Amount</u>	<u>% /b</u>	<u>Amount</u>	<u>% /b</u>
<hr/>						
FY81						
April-June	1981		9.0	9.0	0.0	0.0
FY82						
July-September	1981		10.5	19.5	6.0	6.0
October-December	1981		11.5	31.0	7.0	13.0
January-March	1982		12.5	93.5	8.0	21.0
April-June	1982		13.0	56.5	9.0	30.0
Subtotal			<u>47.5</u>	<u>56.5</u>	<u>30.0</u>	<u>30.0</u>
FY83						
July-September	1982		12.5	69.0	11.0	41.0
October- December	1982		12.0	81.0	12.0	53.0
January-March	1983		11.0	92.0	10.0	63.0
April-June	1983		8.0	100.0	9.0	72.0
Subtotal			<u>43.5</u>	<u>100.0</u>	<u>42.0</u>	<u>72.0</u>
FY84						
July-September	1983				8.0	80.0
October-December	1983				8.0	88.0
January-March	1984				7.0	95.0
April-June	1984				5.0	100.0
Subtotal					<u>28.0</u>	<u>100.0</u>
<u>Total</u>			<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

/a Assuming the loan would become effective as of March 31, 1981.

/b Percentages are cumulative.

AEP Projects  
October 31, 1980

**KOREA**  
**THE KOREA DEVELOPMENT BANK**  
**ORGANIZATION CHART**  
**(As of March 1, 1980)**



KOREA

THE KOREA DEVELOPMENT BANK

ANNEX C: THE NATIONAL INVESTMENT FUND

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THE KOREA DEVELOPMENT BANK

ANNEX C: THE NATIONAL INVESTMENT FUND

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THE KOREA DEVELOPMENT BANK

ANNEX C: THE NATIONAL INVESTMENT FUND

Establishment of the National Investment Fund

1. The National Investment Fund Law was enacted in late 1973 and the National Investment Fund (NIF) commenced operations on January 1, 1974. The purpose of the Fund is to channel a part of Korea's domestic savings into long term financing of investment in priority sectors. Prior to the establishment of the NIF there was little long-term domestic currency financing available in Korea as commercial banks were averse to making term loans. Consequently, business enterprises had either to rely on frequent roll-over of short-term loans or to borrow long-term foreign currency resources domestically or abroad. The NIF was set up to fill this obvious gap in the financial system and has become the major source of domestic currency long-term funds in the economy. As of end 1979, NIF funded term loans accounted for a very large share (30.5%) of all outstanding equipment loans/1 made by KDB and the DMBs (Table 1).

Organization

2. The annual financing and operations program of the NIF is determined by the Ministry of Finance (MOF) although administrative matters are handled by the Bank of Korea (BOK). Disbursement of NIF loans to qualifying borrowers is administered by all banking institutions except the Citizens National Bank, the Korea Housing Bank and the foreign commercial banks. The legal administrator of the Fund is the National Investment Fund Management Committee (NIFMC) which is chaired by the Prime Minister and comprises several cabinet members including the Minister of Finance, the Governor of the BOK, the Governor of KDB and three representatives from the private sector. The NIFMC establishes the operating criteria of the Fund, the annual financing and operations program and approves its financial accounts.

Funding

3. The NIF is funded through the issuance of National Investment Bonds. The magnitude of annual sales of NIF bonds and the financial regulations pertaining to the issuance of NIF bonds is determined by the MOF. The ceiling on the total value of bonds issued annually is subject to the approval of the National Assembly. The maximum interest rate payable on the NIF bonds is equal to the interest rate payable on one-year time deposits i.e. 24% since January 1980. NIF bonds are not sold to the general public.

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/1 In domestic and foreign currency.



The major subscribers to NIF bonds are banking institutions, savings associations and non-life insurance companies. By law, banking institutions have to invest, on a monthly basis, a given percentage of the net increase in their time and savings deposits in NIF bonds. When the NIF program started banking institutions /1 were required to invest 20% of the net increase in their deposits in NIF bonds. This percentage was later lowered to 15% and currently stands at 13%. Nonlife insurance companies are required to invest 50% of their net insurance premiums in NIF bonds. In addition to the forced contribution of banking institutions, public funds are also allocated to NIF. Banking institutions, savings associations and nonlife insurance companies accounted for 59.0%, 13.4% and 5.5% respectively of the 1979 increase in NIF funds (Table 2)./2 The remaining 22.1% came from public funds./3 The comparable figures for 1978 were 65.9%, 8.6% and 7.8% respectively with public funds accounting for 17.7%.

#### Lending Rates

4. In early 1980, NIF loans for general purposes /4 with a maturity of up to three years carried an interest rate of 21% and loans with a maturity of 3-8 years carried an interest rate of 22%. Comparable lending rates for nonpriority borrowers were 24.5% and 25.5% respectively in the case of equipment loans financed with resources other than NIF. The NIF loans made by commercial banks could be rediscounted with NIF at rates of 19.5% for less than 3-year maturities and 20.5% for 3 to 8-year maturities. Applicable rates for rediscounting of NIF loans by KDB were respectively 20.5% and 21.5%. The spread accruing to the commercial banks on NIF loans was consequently 1.5% but was only 0.5% for KDB. The difference between the

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/1 Excluding the National Agricultural Cooperatives Federation and the Central Federation of Fisheries Cooperatives.

/2 Excluding repayments from previous NIF loans which are carried forward.

/3 Public funds comprises resources from government municipalities, Public officers pension funds, Veterans Pension Fund and Export Insurance Fund.

/4 As opposed to loans for agriculture, exports and shipbuilding whose lending rates are more heavily subsidized.

yield payable on NIF bonds (24%) and the rate at which the proceeds are lent to the financial institutions (19.5% to 21.5%) constitutes a negative spread of 3-4%./1 This interest rate differential represents, aside from other administrative expenses, the cost to the Government of operating the NIF program.

#### Institutional Allocation of NIF Funds

5. NIF loans are channelled through the nationwide commercial banks, the specialized banks /2, the local banks and KDB. As of December 31, 1979, 81.8% of NIF loans outstanding had been channeled through the specialized banks and KDB /3, 16.0% through the commercial banks and 2.2% through the local banks (Table 3). KDB was by far the most important lender of NIF resources accounting for 65.9% of all NIF loans outstanding as of end 1979. The Korea Export-Import Bank came next and accounted for 4.8% of NIF loans outstanding. Tables 2 and 3 show that there is no one to one relationship between the contribution of individual financial institutions to funding the NIF and their allocation of NIF loans. In some instances, institutions contributing to NIF are not permitted to allocate NIF funds as is the case with the Citizens National Bank.

#### Sectoral Allocation of NIF Funds

6. The allocation of NIF funds among broad economic sectors is determined by the MOF while the allocation of loans within sectors often at a firm specific level is directed by the NIFMC. Some loans are preallocated in terms of both specific borrower and amount while in other cases only the borrower is designated. Total NIF loan allocations in 1980 are expected to amount to W 538 billion. Of this amount, 72% (W 387 billion) have been preallocated to specific borrowers with a predetermined loan amount while 10.6% (W 57 billion) have been preallocated to specific borrowers only. Consequently, only 17.4% of all NIF loans in 1980 can be allocated at the full

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/1 Based on total outstanding NIF loans at end-1979, a subsidy of 3-4% represents a total annual subsidy of about \$85 million which is financed out of budgetary allocations.

/2 Except CNB and the Korea Housing Bank.

/3 Korea Development Bank (65.9%), Korea Export-Import Bank (4.8%), Agricultural Cooperatives (4.4%), Small and Medium Industry Bank (2.9%), Korea Exchange Bank (2.7%), and the Fisheries Cooperatives (1.1%).

discretion of the financial intermediaries. In the majority of cases, when the borrower and amount has been predetermined the financing institution does not carry out an independent project appraisal but merely operates as a conduit for channeling NIF funds. Given the magnitudes involved, the allocating mechanism employed is crucial to the success of the NIF program. At present, relatively little is known about how specific borrowers are identified and how the magnitude of individual loans is determined by the NIFMC.

7. In terms of sectoral allocation, heavy industries and power accounted for 63% and 26% respectively of NIF loans outstanding as of end 1979. The remaining 11% went to finance exports by deferred payment (4.8%), food production (4.2%), Saemaeul factories (1.4%) and fishing and mining (0.6%). Heavy industries are clearly a major recipient of NIF funds. The support provided to these industries by NIF takes many forms: NIF loans to specific heavy industries can be made for financing factory construction and for the production of capital goods; NIF loans can also be made to other industries in order to finance the purchase of the same machinery.

#### Proposed Modifications of NIF

8. There is no doubt that with NIF outstanding loans accounting for as much as \$2.5 billion or 30.5% of all equipment loans by DMBs and KDB at end-1979 and with annual appropriations reaching over \$1 billion in 1980, the NIF Program has achieved a substantial transfer of resources to the industrial sector. In fact, the very size of this subsidized lending program which should normally be earmarked for priority activities seems questionable. It is doubtful that as much as 30% of all industrial investment really needs to be subsidized. Indications are that the availability of subsidized financing has sometimes led to overinvestment in certain branches of industry. At present NIF provides loans to various sectors for a variety of purposes. On the one hand, NIF loans finance the production of goods in priority sectors while other NIF loans are used to finance the purchase of, conceivably, the same goods. In addition, a significant proportion of NIF funds are preallocated and there appears to be no clearly defined allocation criteria. Priority sectors eligible for NIF subsidized funding are too broadly defined and, as a consequence, NIF lending accounts for too large a share of total term lending. For these reasons, it is proposed that, over time, the scope and magnitude of NIF lending be reduced so that the program be better focused in terms of both the type of projects financed and the type of financing provided.

9. A redefinition of priorities is needed with a view to reducing the sectoral scope and magnitude of NIF lending and giving the program a better focus. Having reduced the sectoral scope of NIF, it is also recommended that the institutional scope be reduced. To this end, NIF funds should be channeled through specialized banks and KDB only. An additional benefit of

this concentration of NIF lending would be to free the commercial banks of NIF operations and of the attending government dictations. The commercial banks would then be in a position to allocate their own funds on market oriented criteria. The specialized banks and KDB would be in a better position than commercial banks to allocate NIF funds as they already have well developed project appraisal/supervision capabilities for term lending. Resource allocation to individual projects is therefore likely to be more efficient particularly if accompanied with a reduction in the extent of government directed allocations at a firm specific level. In addition to project appraisal, KDB which is the main handling bank for NIF should be asked to undertake specific sector/subsector studies with a view to better defining and restricting specific priority subsectors for NIF funding.

10. The NIF program can be confined to KDB and the specialized banks without reducing its present geographical reach. Although their branch network is not as developed as that of the commercial banks, KDB and SMIB together have a very wide branch network. KDB currently has 10 branch offices with at least one KDB office in each of the provinces. SMIB has an extensive and expanding branch network with well over 100 branches. Under normal conditions, the larger NIF clients would go to KDB while small and medium industries would apply to SMIB. If, however, a large client were unable, for geographical reasons, to work with KDB directly then KDB might be permitted to ask SMIB or another specialized bank to handle NIF funds on its behalf. Alternatively, KDB might request a conveniently located commercial bank to operate as a conduit for NIF funds. On a priori grounds, however, such instances are likely to be limited.

11. The "one bank" tradition in Korea provides an argument against removing NIF operations from commercial banks. It seems however that the main bank to which the client firm's collateral is pledged could issue a guarantee to the institution from which NIF funds are being borrowed to cover the amount of the NIF loan considered. Conceptually, this procedure would be similar to the one currently adopted when a firm "graduates" from small to large /1 and therefore has to change its source of finance from SMIB to KDB.

#### Further Study of NIF Program

12. In order to help restructure the NIF program, some further information is required on the existing program and on some key related issues. Some areas of further study are mentioned below:

- (a) asset size of NIF clients;
- (b) number of loans/clients financed by the specialized banks, KDB, and commercial banks and extent of clientele overlap;

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/1 i.e. when employment reaches 300 employees and assets exceed W 500 million.

- (c) regional spread of clients;
- (d) level of arrears on NIF funded loans by commercial, specialized banks and KDB;
- (e) administrative costs of processing NIF loans by commercial, specialized banks and KDB;
- (f) processing time taken by the commercial banks, specialized banks and KDB;
- (g) maturity structure of NIF loans by commercial banks, specialized banks and KDB;
- (h) based on subsectoral priorities and comparative advantage of Korean firms, need for and magnitude of the interest subsidy, if any, that needs to be provided on NIF funds; and
- (i) proportion of the net increase in time and saving deposits which will have to be invested in NIF bonds by banking institutions given the decision to reduce the magnitude of the program and given the growing volume of funds generated by repayments of earlier NIF loans.

13. Detailed terms of reference of an NIF study would be discussed at negotiations. The study could be undertaken jointly by KDB and other government agencies concerned with the NIF program.

KOREA

INDUSTRIAL FINANCE SECTOR LOAN

THE NATIONAL INVESTMENT FUND

Outstanding Equipment Loans by Source of Funds  
(Won billion)

	1978				1979			
	DMBs Amount	KDB Amount	Total Amount	%	DMBs Amount	KDB Amount	Total Amount	%
<u>Source of Funds</u>								
National Investment Fund	273.8	528.5	802.3	36.4	348.4	803.4	1,151.7	30.5
Banks' own resources	818.8	-	818.8	37.1	1,208.6	-	1,208.6	32.1
Govenment budgetary allocations	147.4	220.4	367.7	16.7	194.2	611.1	805.3	21.4
Foreign currency resources	108.9	107.6	216.6	9.8	130.2	473.7	603.9	16.0
<u>Total</u>	<u>1,348.9</u>	<u>856.5</u>	<u>2,205.5</u>	<u>100.0</u>	<u>1,881.4</u>	<u>1,888.1</u>	<u>3,769.5</u>	<u>100.0</u>

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KOREA

INDUSTRIAL FINANCE SECTOR LOAN

THE NATIONAL INVESTMENT FUND

Operations of the National Investment Fund in 1977-80  
(Won billion)

Source of Funds	1977	1978	1979	1980/ <u>c</u>	Uses of Funds	1977	1978	1979	1980/ <u>c</u>
National Savings Associations	17.0	26.4	39.0	32.0	Heavy & chemical industries	118.5	222.6	285.2	365.0
Trust funds of various public entities	43.3	54.6	64.4	74.0	Electric power	40.0	92.0	100.0	120.0
Banking institutions	195.8	202.7	172.3	260.0	Food production	10.0	14.9	19.8	23.0
Insurance	18.1	24.1	16.2	32.0	"Saemaul" plant construction	2.8	3.4	4.7	-
Others <u>/a</u>	37.8	146.5	163.5	140.0	Exports by deferred payment	30.0	29.7	30.0	30.0
					Others <u>/b</u>	110.7	91.7	15.7	-
<u>Total</u>	<u>312.0</u>	<u>454.3</u>	<u>455.4</u>	<u>538.0</u>	<u>Total</u>	<u>312.0</u>	<u>454.3</u>	<u>455.4</u>	<u>538.0</u>

/a Includes repayments and carry over from the previous year.

/b Carry over to the next year.

/c Planned operations.

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KOREA

INDUSTRIAL FINANCE SECTOR LOAN

THE NATIONAL INVESTMENT FUND

Outstanding N.I.F. Loans by Banking Institutions  
(in won million)

As of December 31	1979	
	Amount	%
<u>Nation-wide Commercial Banks</u>	<u>196,615</u>	<u>16.0</u>
Choheung	29,427	
Sangup	39,742	
Cheil	24,779	
Hanil	47,821	
Seoul	54,846	
<u>Specialized Banks (incl. KDB)</u>	<u>1,004,974</u>	<u>81.8</u>
Korea Development Bank	809,125	(65.9)
Korea Exchange Bank	33,759	(2.7)
The Medium Industry Bank	35,306	(2.9)
The Agricultural Cooperatives	53,629	(4.4)
The Fisheries Cooperatives	13,485	(1.1)
The Korea Export-Import Bank	59,670	(4.8)
<u>Local Banks</u>	<u>26,823</u>	<u>2.2</u>
Pusan	11,755	
Taegu	2,334	
Kyongnam	9,587	
Others	3,147	
<u>Total</u>	<u>1,228,412</u>	<u>100.0</u>

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KOREA

INDUSTRIAL FINANCE SECTOR LOAN

THE NATIONAL INVESTMENT FUND

Outstanding N.I.F. Loans by Sector at End 1979  
(in won million)

	Amount
<u>Heavy Industry</u>	<u>782,011</u>
Purchase of local machinery	102,269
General machinery	43,924
Plant	57,402
Newly developed machinery	943
Construction of machinery factory	139,435
Large scale	47,123
Special machinery	3,578
Government specified	43,238
Special steel	13,653
Chang-Won industrial complex	30,068
Others	1,775
Planned shipbuilding	81,760
Defense Industry	78,542
Other heavy industry	380,005
Steel	59,044
Shipbuilding	32,236
Chemicals	128,098
Electronics	15,685
Construction of industrial complex	61,102
Others	82,840
<u>Food Production</u>	<u>51,402</u>
Purchase of farm machinery	34,196
Others	16,845
Fishing	127
Mining	234
Electric Power	317,500
Saemaoul Factory	17,829
Exports by Deferred payment	59,670
<u>Total</u>	<u>1,228,412</u>